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NEGOTIATION OF UNITED STATES-CANADA FREE TRADE AGREEMENT

ORIGINAL

HEARING

BEFORE THE

COMMITTEE ON FINANCE
UNITED STATES SENATE

NINETY-NINTH CONGRESS

SECOND SESSION

APRIL 11, 1986

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PROPOSED NEGOTIATION OF UNITED STATES-CANADA FREE TRADE AGREEMENT

FRIDAY, APRIL 11, 1986

U.S. SENATE,
COMMITTEE ON FINANCE,
Washington, DC.

The committee met, pursuant to notice, at 9:30 a.m., in room SD-215, Dirksen Senate Office Building, Hon. Bob Packwood (chairman) presiding.

Present: Senators Packwood, Danforth, Chafee, Heinz, Symms, Grassley, Long, Bentsen, Moynihan, Baucus, Mitchell, and Pryor.

[The press release announcing the hearing and the opening statements of Senators Wallop, Grassley, Mitchell, and Stennis follow:]

[Press Release No. 86-022]

FINANCE COMMITTEE ANNOUNCES HEARING ON NEGOTIATION OF UNITED STATES-CANADA FREE TRADE AGREEMENT

Senator Bob Packwood (R-Oregon), Chairman of the Senate Committee on Finance, announced that the committee will conduct a hearing on April 11, 1986 on the Administration's stated desire to enter into bilateral trade negotiations with Canada. The hearing will begin at 9:30 a.m. in Room SD-215 of the Dirksen Senate Office Building.

Chairman Packwood noted that on December 10, 1986 President Reagan notified the Committee of the Administration's desire to accept Canadian Prime Minister Mulroney's proposal to undertake trade negotiations "on the broadest possible package of beneficial reductions in barriers to trade in goods and services."

Senator Packwood stated, "Under the Trade Act of 1974, the Finance Committee is responsible for authorizing the initiation of bilateral trade negotiations leading to any trade agreement which reduces or eliminates U.S. import duties. The President's historic proposal to enter into such negotiations with Canada, our largest trading partner, raises a host of important and difficult issues which the Committee must consider. This hearing is part of a process by which the Committee can reach an informed judgment on the merits of the President's proposal."

PREPARED STATEMENT OF CHUCK GRASSLEY

Mr. Chairman, the Administration has referred to this agreement as an "historic opportunity" for the bilateral interests of our two countries. And while it may be such an opportunity, I for one feel this committee should weigh the proposal to pursue such negotiations carefully before a final decision is made.

As you might expect, coming from an agricultural state, I have some serious concerns with Canada's agricultural trade policies. On the one hand, Canada's nontariff barriers require live hogs imported from the United States to be subjected to a 30 day quarantine which make live hog exports to Canada un-economical. And yet on the other hand, the Canadians subsidize their pork imports into this country, therefore further eroding the base by which our hog growers can compete.

Mr. Ambassador, with the serious problems we in the Midwest are experiencing in the farm economy today, it would be my hope that you will be able to give me some assurance this morning that any agreement between our two countries will not work against U.S. agricultural export interest. In particular, I would hope that any agreement reached would not, on the one hand, remove U.S. trade restrictions but not Canadian restrictions. Additionally, I would hope we will not allow deals with border measures so that certain Canadian domestic subsidy practices continue to provide an unfair competitive edge to Canadian producers.

While I personally have some strong concerns regarding the possible adverse impact of such an agreement on the U.S. agricultural sector, there are also others on the committee who have strong concerns about Canadian lumber subsidies, telecommunications, intellectual property rights in motion picture and television programming, and Canadian investments. All of these I believe need to be resolved in some satisfactory manner if we are to have a meaningful trade agreement.

As everyone is aware, two-way trade between Canada and the United States exceeded 112 billion dollars in 1984, and represents the largest trading relationship in the world. In fact the United States exported more to the Province of Ontario in 1984 than it exported to Japan. However, as with Japan, the United States is currently running a huge trade deficit. In fact, in 1984 for example, the United States recorded a 19.9 billion dollar trade deficit. And while I realize that our current account deficit is much smaller at 6.1 billion dollars, I believe we need to concern ourselves with how we go about reducing these figures.

Mr. Chairman, Mr. Ambassador, I would like to conclude on a positive note by stating that the United States should certainly give serious consideration to a free trade agreement with Canada. But I do believe that a decision to proceed should not overlook the need to get a mutually agreeable resolution of these issues. We can ill afford to put our industrial and agricultural interests at any further competitive trade disadvantage, and I for one will be following these discussions to make sure this doesn't happen.

STATEMENT OF SENATOR GEORGE J. MITCHELL

The United States and Canada share the largest bilateral trade relationship in the world. We have a long history of friendship and cooperation. For these reasons, a bilateral free trade agreement offers tremendous opportunity for benefit on both sides.

But even among friends, delicacy is needed in dealing with matters of international trade. It seems certain that Canada will benefit from a trade agreement with the U.S., simply by enjoying greater access to the enormous American market. How the U.S. benefits from an agreement, on the other hand, depends greatly on how we negotiate and structure such an agreement. It is vital that in crafting a free trade pact, we show sensitivity to the regional and sectoral impacts it will have.

Nowhere is this need for sensitivity more important than in Maine, which enjoys a variety of economic and commercial ties with Canada. Because Canadian tariffs are on average higher than American tariffs, one might expect that a simple bilateral elimination of tariffs could benefit a state in such proximity to Canada. Unfortunately, the bilateral trade problems faced by Maine's major industries have little to do with tariffs, or other obstacles at the border. They have everything to do with Canada's social policy of subsidizing favored industries.

Let me describe the most salient cases from Maine's point of view. Bilateral trade in potatoes is already nominally free. Yet, potato growers in New Brunswick and Prince Edward Island receive far more government assistance than those in Maine. This subsidized competition is crippling an already depressed industry, and is not fair trade. The issue of Canadian subsidization of potatoes needs to be addressed in free trade negotiations, or those issues will be meaningless for Maine's potato farmers.

A further problem lies in the fact that many of the Canadian subsidies are provided by the provinces, in addition to the federal Canadian government. Ways of dealing with widespread provincial subsidy practices must be found. To my mind, this is not an issue that has been adequately addressed to this date. We must be clearer on how the provinces will participate in a free trade agreement, or a large potential source of benefits will be lost.

The lumber industry faces a predicament similar to that of the potato industry. The Canadians have long been aware of our unhappiness with their subsidization of stumpage, and we have been negotiating the issue with them for some time. But thus far we have made little progress, and this raises a larger question about this administration's willingness to bargain effectively with Canada. Despite constant prompting from Congress, the administration has insisted on softpedalling lumber issues, and the Canadians know this. Thus, they have no incentive to make concessions. When the Canadians know *in advance* that the U.S. is not willing to take strong action if concessions are not forthcoming, they have no incentive to move. I hope this does not become a pattern in future negotiations.

Fishing, a third important Maine industry, is in a slightly different position than the lumber and potato industries. Maine fishermen are also victims of unfair competition in the form of Canadian subsidies; however, sharp differences, both philosophical and practical, between American and Canadian fisheries management systems pose a problem which underlies many of the industry's trade issues.

The market for North Atlantic fish is still not well-developed, because of the exceptionally perishable nature of fish and variations in the overall supply of fish in the sea. New England's first display auction for fish will be opening soon in Portland, Maine. It has been ten years in the making, and is a bold, innovative effort to solve some of these problems.

Industry leaders are also seeking to address the scientific basis of the respective Canadian fisheries management systems. Professor James Wilson of the Economics Department of the University of Maine is hoping to organize an academic conference in the fall under the auspices of the New England Fisheries Management Council and the University of Maine to begin to resolve differences in that area. Professor Wilson is a close observer of American Canadian trade issues, especially as they affect the fishing industry—and I wish to submit for the record a copy of comments which he recently submitted to me.

However, the major point I wish to make is that the market for fish is a tenuous one. Opening it up for free trade at this time is unlikely to benefit either the United States or Canada—especially while efforts to address basic issues of resource management are still in early stages.

This is also the position of the Maine Sardine Council and other industry leaders, who see much to lose in the free trade talks and not much gain.

Fishing issues must be dealt with independently of free trade issues. If the United States chooses to do anything less than that, then it is extremely important that basic resource management issues be addressed concurrently—and that they not be minimized or shortchanged.

My second point relative to fishing is that even under any free trade agreement, American fishermen must not lose the right to pursue legal redress in instances of unfair competition from Canadian industry subsidies. Currently, New England fishermen are awaiting the ITC's final decision in a countervailing duty petition on Canadian groundfish imports. Continued and aggressive enforcement of U.S. antidumping and countervailing duty laws is an important right and protection. No agreement should alter these GATT-sanctioned processes.

Finally, I want to mention two more issues that do not involve specific industries but, which are important to the success of a bilateral trade agreement. First, I note that virtually *all* industries that do trade with Canada have complained that the U.S. dollar is grossly overvalued against the Canadian dollar. This constitutes a barrier to U.S. exports of the first rank, as well as exacerbating the inflow of imports. Earlier this year, the U.S. joined in a multilateral effort to adjust the dollar's value against other major currencies. Free trade talks afford us an ideal opportunity to begin addressing exchange rate management vis-a-vis Canada.

Second, to assist in the resolution of trade disputes, I introduced legislation last August which would create an International Joint Economic Commission. This commission would both serve as an objective fact-finding body, and give advisory opinions on issues referred to it by both governments. I believe this commission could enhance the quality of the economic relationship between the U.S. and Canada by helping to resolve issues in a fair and impartial manner. Such a commission could also advise the two governments on those issues—such as natural resource issues, or social policies—on which a different bilateral approach might be necessary.

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April 9, 1986

To: Joe Damond/Sen. Mitchell
From: Jim Wilson, Prof. of Economics, UMO

At the request of friends in the fishing industry, I am writing with regard to free trade talks with Canada and their impact on the Maine fishing community.

The fishing industries of Canada and the United States can both benefit through freer bi-lateral trade. However, this can only happen if care is taken to create market institutions appropriate to the industry. Let me explain my point:

The basic idea of free trade assumes that efficient markets are in place to carry out the individual exchanges that constitute the trade. For most products, especially manufactured products, the existance of adequate markets is not a problem. Ordinary commerical law adequately governs trade in these instances. Private contracts can be widely initiated and enforced. There is no need for special trading rules or institutions.

The rules and institutions in some markets, however, have to be tailored to the needs of their particular products. Trading based on normal commerical law tends to lead to very inefficent markets in these kinds of products. In the fishing industry peculiar problems such as perishability, very subtle but important quality variations and irregular supplies (due to weather, fish migrations, and so on) create special requirements for efficient markets.

In the current (inefficent) market:

Perishability, for example, means that trading must take place very rapidly; product cannot be inventoried; it cannot wait in transit while a buyer is found; and it requires special handling facilities fitted to the peculiar requirements of fish. Buyers and sellers can only avoid perishability problems by trading with people they have dealt with many times before; they can't trade widely; they can't search the entire East Coast to find a more opportune buyer.

The subtle but important variations in quality mean that a buyer cannot buy from any seller in the market (and visa versa). He must know the seller, know what the seller means by a particular description of product quality and must have a means for enforcing representations about product quality. This means that buyers must have a long standing, mutually dependent relationship with sellers. If a seller misrepresents the product to the buyer, the buyer (at a minimum) has to know that such misrepresentation will be costly to the seller as well as to himself. Normal contracting procedures are almost pointless in this kind of market; contracts cannot be enforced and would be exceedingly expensive to write on a continuing basis. Consequently, buyers effectively wind-up trading with only a small number of sellers whom they've learned they can trust.

But trading with only a small number of sellers creates its own problems. First, it makes buyers very vulnerable to the irregularity in supplies that can occur, for example, if one or two boats have mechanical problems. This vulnerability to irregular supplies means that buyers (processors) cannot contract in the final market with reasonable certainty and that they are frequently forced to hustle fish on a non-contractual and usually low price basis. In effect, they cannot develop the market and, because of the conditions of sale that they are frequently forced into, they cannot obtain the price for the product that they might otherwise be able to.

Second, this method of sale means that a buyer must buy all the fish a fisherman (his regular supplier) has for sale. A large part of this fish must be resold to other buyers (time consuming and often difficult to do) or it must be allocated to lower quality salt fish or even fish meal. The buyer not only frequently loses money on these resales but also is forced to expend a great deal of time on the process.

Finally, under this system there is no way for the buyer to pay higher prices for good quality and lower prices for poor quality fish. A cod is a cod is a cod (but not much like a rose). This means that fishermen do not have a financial incentive to deliver high quality fish (to do so requires costly extra handling). Lower and much more variable quality product creates even more difficult problems for processors when it comes to contracting in final markets and is a major factor retarding consumption of fish.

In Maine we are trying to attack these problems with the new fisheries display auction in Portland. The point of the auction is:
1. to consolidate supplies of fish in order to reduce irregularities in supply,
2. to display fish before purchase so that prices can reflect quality.

3. to allow sellers and buyers access to each other without having to build up years of 'trustworthy' relationships (the quality of displayed fish will speak for itself),
4. to eliminate the need for resales by selling fish in relatively small lots, and
5. to clear the market in one single hour during which all sales are made for the day.

It has taken us nearly ten years - from the time the idea of the auction was first developed until today - to get this auction going. It has required the cooperative and very creative efforts of people in State government, in the Congressional delegation (leaning very heavily on EDA), the University and, especially, the city government and the industry. (Incidentally, NMFS did not assist at all in the project.)

Internationally these kinds of specialized markets, such as are required in the fishing industry, are not now in place and are not likely to arise spontaneously simply because of a new, freer trade environment. In the absence of such markets, industries such as the fishing industry will not benefit from freer bi-lateral trade.

The need for specialized markets does not constitute an argument against free trade talks with Canada nor is it necessarily a reason for the fishing industry to be excluded from those talks. The need for specialized markets really argues for deliberate consideration of a bilateral mechanism (or commission such as you have earlier proposed) for the purpose of first identifying and then implementing the necessary institutional changes in these markets. The commission function I am suggesting here is not one of mediating or resolving disputes (also necessary), rather what is required is a commission that can (1) anticipate the areas or particular markets (such as fisheries) where new bi-lateral market institutions would be useful and (2) facilitate the creation of such institutions - an often very time consuming process as the Maine experience with the auction illustrates.

In the context of freer trade with Canada this would mean giving special consideration to industries like fishing - not to exclude them from the free trade discussion - but simply because these industry can gain from freer trade only if specialized markets are created. In other words, I am suggesting a secondary forum where the particular needs of industries such as fishing can be addressed.

STATEMENT BY SENATOR JOHN STENNIS

Mr. Chairman, thank you for allowing me to address this committee on a most critical situation facing our nation today. Of course, I am talking about the trade situation with our closest friend and ally, Canada.

As long as I can remember, we have enjoyed the best of relationships with our neighbors to the North, and I expect that relationship to continue well into the future. However, in order to insure a continued strong friendship, we need to keep all communication lines open and work for trade agreements that benefit both countries.

It is good that our President and his representatives want to enter into bilateral trade negotiations with Canada in order to "hash out" a free trade agreement between the two countries. But, Mr. Chairman, I am concerned that, perhaps, the President does not take seriously enough, the current situation relating to the importation of Canadian timber products into the United States.

It should be clear to everyone by now that the Canadian government is unfairly subsidizing their timber industry by reducing the stumpage rates in government forests, which I understand constitute about 95 percent of all forests in Canada. No one knows better than you, Mr. Chairman, what devastating effects this unfair action is having on our own timber industry.

From Oregon to Mississippi to Maine, lumber mills are closing down and log trucks have quit rolling. In my own home town, I know people who have been extremely successful in the timber industry in the past and who have now been forced to put locks on their equipment and buildings. If I felt that this was caused by their inefficiency or poor management, I would not be here today. However, I know them to be capable and skilled in their work, and yet they are being forced out of the industry by not being able to compete with subsidized Canadian imports.

It is my opinion, Mr. Chairman, that the most critical trade issue with our Canadian friends is this issue of timber subsidies. Until that issue is resolved, or at least given priority attention, I do not think we should move ahead with any other negotiations. We have passed resolutions and spoken for hours on the floor of the Senate, and yet there is no evidence of any positive action. I will not give up and I hope that the Administration will join us immediately in this fight for fairness.

Thank you.

The **CHAIRMAN**. The committee will come to order, please.

We are shifting today from the tax bill to a hearing on the subject of a potential Canadian-American free trade agreement. I have spoken with the Special Trade Ambassador, Ambassador Yeutter, many times; and I have warned him that there is the possibility that this committee, including myself, is going to vote to turn down the request for fast-track legislation because we have had nothing but vague promises and unsatisfactory responses from the Canadian Government on a variety of areas.

In my State, I have a particular interest in timber. Other States have a particular interest in gas. Others have a particular interest in uranium. And we have gotten no satisfactory responses from the Canadian Government that they really want to negotiate to end their subsidies and to enter into a genuine free trade agreement.

And I think there are enough members on this committee that feel reluctant to start down any road at all without having some further indication of what we might find at the outcome, that next week when we vote on this resolution—and we will vote on it midweek or later in the week, next week—as to whether or not to approve or disapprove the authority of the administration to go forward on these negotiations.

It is my prediction that if we were voting today, we would vote to turn that authority down; and I don't think that there is much that can be done between now and that vote to turn this committee around, short of a conversion almost like salt on the road to Damascus, and that has happened once in history. And maybe it could happen with the Canadians next week; but absent that, it would be my recommendation to the committee that we vote to turn down the authority to negotiate on a fast-track basis. And I think the committee would agree with that conclusion.

Senator Baucus.

Senator **Baucus**. Mr. Chairman, I very much appreciate your statement. I think it reflects the concern of most members of this committee, that is, that Canada very much wants a free trade agreement. It desperately wants a free trade agreement.

The fact of the matter is that various industries in Canada have expended tremendous sums of money trying to get a free trade agreement with the United States. I know the timber industry in Canada has spent about $5 million lobbying in the United States. They want a free trade agreement. They have got a good deal now; they want a better deal.

In fact, Prime Minister Mulroney at the House of Commons on March 21 said that Canada wants a bigger market share of forest products in the United States. So, it is clear to me that they are pushing hard to expand their market in the United States the best they can.

At the same time, Canada has a lot more negotiators working on this project than we do. They have 10 to 12, up to 30, negotiators working on this. We, on the U.S. side, have one, two, or three. We are mismatched. Beyond that, our country does not have a good record in negotiating trade agreements. That does not speak disparagingly against any administration; that has been true for all administrations in the last decade. The reasons for that are we don't have the staying power; we don't have the staff on our side; we don't have the sophistication that other countries have. That is basically because our country is not an export-driven economy as other countries. Canada is very much becoming an export-driven economy. They have their natural resources; they want to export the natural resources to the United States. We have to wake up to that and know how to accommodate that.

Now, Mr. Chairman, very simply, it is my strong feeling that in an effort to try to improve our trade relationship with Canada, we vote to disapprove the fast-track but without prejudice, that is, send the signal to the Canadians that, yes, in principle we are in favor of a free trade agreement; we think it is a good idea in principle; but there are too many unanswered questions. There are too many sectors that have not been sufficiently addressed; that we don't yet have our ducks in a row.

So, at this point, we will disapprove, but disapprove without prejudice, so that we can iron out some of those difficulties and get a better idea of where we are so that, hopefully, we can negotiate on down the road a free trade agreement. Mr. Chairman, later on in this hearing, I will be presenting some charts to show what some of the economic problems are between the United States and Canada.

At this point, it is my strong recommendation that this committee vote to disapprove the fast-track but without prejudice. Thank you.

The **Chairman**. Senator Grassley, then Senators Mitchell, Long, Danforth, and Symms.

Senator GRASSLEY. Mr. Chairman, thank you. The administration has referred to this agreement as an historic opportunity for bilateral interests of our two countries. And while it may be such an opportunity, I, for one, feel that this committee should weigh the proposal to pursue such negotiations carefully before a final decision is made; in other words, move on a very slow track.

As you might expect, coming from an agricultural State, I have some serious concerns with Canada's agricultural trade policy. On the one hand, Canada's nontariff barriers require live hogs imported from the United States to be subjected to a 30-day quarantine, which make live hog exports to Canada uneconomical. And yet, on the other hand, the Canadians very openly subsidize their pork imports into this country, therefore eroding the base by which our hog growers can compete. Mr. Ambassador and Mr. Chairman, with the serious problems we in the Midwest are experiencing in the farm economy today, it would be my hope that you will be able to give me some assurances this morning that any agreement between our two countries will not work against U.S. agricultural export interests.

Particularly, I would hope that any agreement reached would not, on the one hand, remove United States trade restrictions, but not Canadian restrictions. Additionally, I would hope we will not allow deals with border measures so that certain Canadian domestic subsidy practices continue to provide an unfair competitive edge to Canadian producers. While I personally have some strong concerns regarding possible adverse impact of such an agreement on the United States agricultural sector, there are also others on the committee who have strong concerns about Canadian lumber subsidies, telecommunications, intellectual property rights in motion picture and television programming, and Canadian investments.

All of these, I believe, need to be resolved in some satisfactory manner if we are to be able to have any meaningful trade agreement. As everyone is aware, two-way trade between Canada and the United States exceeded $112 billion in 1984 and represents the largest trading relationship in the world. In fact, the United States exported more to the Province of Ontario in 1984 than it exported to Japan. However, as with Japan, the United States is currently running a huge trade deficit. In fact, in 1984 alone, for example, the United States reported an almost $20 billion trade deficit. And while I realize that our current account deficit is much smaller at $6.1 billion, I believe we need to concern ourselves with how we go about reducing these figures.

So, Mr. Chairman and also Mr. Ambassador, I would like to conclude on a positive note by stating that the United States should certainly give serious consideration to a free trade agreement with Canada; but I do believe that a decision to proceed should not overlook the need to get mutually agreeable resolutions of these issues. We can ill afford any more to put our industrial and agricultural interests at any further competitive trade disadvantage; and I, for one, will be following these discussions to make sure that that does not happen.

The CHAIRMAN. Senator Mitchell.

Senator MITCHELL. The United States and Canada share the largest bilateral trade relationship in the world; and our two countries have a long history of friendship and cooperation. For these reasons, a free trade agreement would appear to offer some opportunity for benefit on both sides, but in the current context it raises deep concerns.

Canada will surely benefit from a free trade agreement with the United States simply by enjoying greater access to the enormous American market. How the United States benefits from such an agreement, on the other hand, depends on how such an agreement is negotiated. It is crucial that any agreement deal with the regional and sectoral impacts it will have. Unfortunately, neither the administration nor the Canadian Government has demonstrated sufficient concern in that regard to date; and as a result, many members of this committee are not prepared to authorize such negotiations on a fast track. Nowhere is this concern greater than in my own State of Maine, which enjoys a variety of economic and commercial ties with Canada.

Because Canadian tariffs are on average higher than American tariffs, one might expect that a simple bilateral elimination of tariffs could benefit a State like Maine so close to Canada. Unfortunately, the trade problems faced by Maine's major industries have little to do with tariffs. They have everything to do with Canada's social policy of subsidizing favored industries. Let me describe the most important cases from Maine's point of view.

First, potatoes. Bilateral trade in potatoes is already nominally free, yet potato growers in New Brunswick and Prince Edward Island receive government subsidies which place them at a competitive advantage with their Maine counterparts. This subsidized competition is crippling an already depressed Maine industry. There once were 3,500 potato farmers in northern Maine. There are now fewer than 1,000; and after this year, when the farmers are receiving prices one-tenth the cost of production, there will be far fewer.

The issue of Canadian subsidization of potatoes must be addressed; and it is complicated by the fact that many of the Canadian subsidies are provided by the provincial governments, in addition to the Federal Government. We just had a recent example of that, Mr. Chairman, that I think serves to illustrate what is wrong with the American attitude in trade. Senator Cohen, who will be our leadoff witness, and I met jointly with the U.S. Secretary of Agriculture to request a modest diversion program to alleviate the depressed conditions in the potato industry. We made a very modest request; not only was our request rejected out of hand, the administration reneged on a prior commitment to produce some limited assistance on border inspection of Canadian potatoes.

And the reason the Secretary of Agriculture of the United States gave us for turning down a request for a diversion program for American potatoes was, he said, we are worried about the Canadian reaction. We don't want to offend the Canadians. At the same time, consider what the Canadians were doing. On February 16, the Provincial government of Prince Edward Island announced a diversion program for their farmers of $6 million. On April 3, the Federal Government of Canada announced a $6 million diversion program for Canadian farmers. On April 9, less than 48 hours after Secretary Ling told us that he wouldn't approve a diversion program for American farmers because he said we are worried about what the Canadians will do, the Federal Government of Canada and the Provincial government of New Brunswick announced yet a third Canadian diversion program for potatoes, amounting to $7 million. So, within a matter of just a few weeks, three separate Canadian diversion programs were announced, while the Secretary of Agriculture of the United States was telling Senator Cohen and I that we don't want to approve a diversion program here for American farmers because we are afraid it is going to offend the Candians.

And that, in a microchasm, illustrates precisely what is wrong with America's approach to trade and particularly in this region. Now, Mr. Chairman, I don't want to take a lot more time. Lumber is another problem. You have touched on it and Senator Baucus has. I won't repeat that. I do want to mention fishing because it is a critical industry in the Northeast. Maine fishermen are also the victims of unfair competition in the form of Canadian subsidies. There, there are also sharp differences—philosophical and practical—in fisheries management systems which poses a problem that underlies the trade issue.

The market for North Atlantic fish is still not well developed, primarily because of the exceptionally perishable nature of fish and variations in the overall supply. Now, we are all trying to improve that circumstance; and I would like to submit for the record a statement by Prof. James Wilson of the University of Maine regarding some aspects of the fish industry problems. The major point I want to make is that the market for fish is tenuous. Opening it up for free trade at this time is unlikely to benefit either the United States or Canada, especially while efforts to address basic issues of resource management are still in the early stages. Fishing issues must be dealt with independently; and if the United States chooses to do anything less than that, basic resource management issues must be addressed concurrently and they must not be minimized by the administration.

Even under a free trade agreement, the American fisherman cannot be permitted to lose the right to pursue legal redress of unfair competition from Canadian subsidies. Currently, New England fishermen are awaiting the ITC's final decision in a countervailing duty petition on Canadian ground fish imports. Continued aggressive enforcement of U.S. antidumping and countervailing duty laws is an important right and protection, and no agreement can be permitted to alter these important processes.

In conclusion, Mr. Chairman, I would like to mention one other minor point—not minor—and that is that, in resolving trade disputes, I introduced legislation last August which would create an International Joint Economic Commission. And if an agreement goes forward, I intend to offer that as an amendment to the agreement. This Commission, patterned after the International Joint Commission, which deals with boundary disputes, would serve as an objective fact-finding body and give advisory opinions on issues referred to it by both Governments. This could enhance the quality of the economic relationship between our two countries by helping to resolve issues in a fair and impartial way and could advise the Governments on these issues, such as natural resources and social policies on which a different bilateral approach might be necessary. I thank you very much, Mr. Chairman, and I join you and Senator Baucus in expressing great concern about proceeding at this time.

The CHAIRMAN. Senator Long.

Senator LONG. Mr. Chairman, it has been my privilege in years gone by to manage some major trade legislation, including the Canadian Auto Parts Agreement, and also the Kennedy round of negotiations, as well as the Tokyo round under President Carter. It seems to me that we are entitled to see a lot more answers and a lot more details than we see here, before we turn this matter loose.

I am satisfied that, once we agree to the fast track, then it is not going to be in the power of anybody here—including anybody on this committee—to keep that matter from sailing through with the support of the President. If we are going to see that American interests are fairly protected, I believe we have to do it before we authorize this fast track. Therefore, because the administration is not in a position to provide the details that we ought to know, on an industry-by-industry basis, where we ought to expect to come out and what this thing will look like when it comes in here on a fast track, I am not willing to vote for it at this point.

As Senator Baucus suggested, I would like to vote for fast track with Canada, but I think that we ought to have a great deal more details than they are in a position to provide us at this point. It is my judgment that, when the fast track comes back in here, if the Canadians need it, they will be able to send their Prime Minister down to talk to the President and their opposite number to talk to our Secretary of State, and I am not even sure that our Special Trade Representative can do what those of us on this committee think he ought to do when it reaches that point.

I suspect he would be instructed by the President, just like anybody the President can instruct would be instructed to do—what the White House thinks, and the White House may be doing what the Secretary of State thinks should be done about it. I am not against Mr. Schulz; I think he is a fine man, but when one takes into account all the defense considerations and all the other considerations that become involved in matters of this sort, it is all too easy to say, "it is all foreign policy."

In the last analysis, the Secretary of State decides such questions rather than the Special Trade Representative; and the President looking at it all can be told, "Well, we don't want to do anything that would adversely affect our good relations with Canada; so, let's go ahead with this thing." If we want to see what the details of it are, I believe that it is beyond our power to agree or disagree when we turn the fast track loose.

I just think we ought to see a lot more of the details before we agree to this matter.

The CHAIRMAN. Senator Danforth.

Senator DANFORTH. Mr. Chairman, it is my understanding that sometime next week, I suppose, we will be voting on a resolution of some sort in the Finance Committee. If there are those who would like to offer a resolution of disapproval of the fast-track authority, we will be voting on that sometime next week?

The CHAIRMAN. That is correct.

Senator **Danforth**. Mr. Chairman, it is my intention to support the resolution of disapproval for authority for a Canadian free trade agreement. I would like to state my reasons for this position. First, Mr. Chairman, I think that it is necessary for the Congress, and especially the Finance Committee, to reestablish some sort of relationship with the administration whereby we again are players in trade policy. I don't think we are now.

I think the situation right now is that Congress has delegated to the President our constitutional responsibility for international trade policy and that the President has so taken over that responsibility that very little is left to the Congress. Now, a number of us have proposals for legislation which we think will improve the situation with respect to trade. Two bills have been reported out of this committee, one relating to Japan, the other relating to telecommunications. Another bill has been introduced with some 34 cosponsors which is an omnibus trade bill.

The position of the administration is quite clear with respect to trade legislation. The administration has said to us, privately, that it is not interested in trade legislation this year, that it wants to stonewall trade legislation. Now, what the administration would like to do is to come to Congress and say to us: Please go along with us; please be flexible; please be docile in meeting the requirements of the administration with respect to trade. But if you have any ideas in Congress, we are not interested in doing business with you.

And I think, Mr. Chairman, that it is necessary at some point for the Congress to be assertive with respect to international trade. Otherwise, we not only don't have power, we don't have credibility. Any statements, any comments coming out of Congress relating to concerns about unfair trade practices of Japan or any other country are discounted. If we never do anything, if we never act, if we never get bills passed, if we can't deal with the administration, if the administration stonewalls us on every issue, and if the administration comes to us and we say, "Oh, fine; the President has taken his position;" then we can never say "no" to the President of the United States.

So, I believe—and this is my strongest reason for my intention to support a resolution of disapproval—I believe that it is necessary for us to begin doing business with the President of the United States and we are not in business right now. The President is stonewalling us.

I think that this is the best time for Congress to be assertive. I agree with Senator Long. If fast track authority is granted, if an agreement is then negotiated with Canada and it comes back to Congress on a take-it-or-leave-it basis, we are going to be under enormous pressure to take it. The President will say 1 year or 2 years have gone into the negotiation. The President has put his reputation on the line, and we can't turn him down. It will be a fait accompli.

So, I believe that the time for us to assert our responsibility is now, not later.

With respect to the refusal of Congress to grant authority at this point, we have existed now for 210 years without a free trade agreement with Canada. I think that we can get on for a few more years. Senator Baucus has stated that there should be a resolution of disapproval without prejudice, for the President to come forward at some future date. The President can always come back to us.

Finally, Mr. Chairman, I am one who doubts that much good will come to the United States from such an agreement. I think the United States has a lot to give, and I think the Canadians will put a lot of pressure on the United States once they start negotiating with us to give a lot. They have indicated that they want us to, in effect, waive our laws on dumping and countervailing duties, and we could do that if we wanted to. We have the power to do that; but when we start pressing the Canadians for any concession or even for fairness in treatment in international trade, the Canadian Government—the Central Government of Canada—tells us that this is a provincial matter. It is not the central government; it is the provinces that have all of these laws restricting American trucking or setting up liquor boards restricting the sale of liquor from the United States or subsidizing products or governing the purchase of telecommunications equipment.

It is the provinces. We, in the central government, they say, can't speak for the provinces. We, in the Congress, can speak for the whole country. It is the supremacy clause of the Constitution. If we are negotiating with Canada, and we are in a position to give a lot, and Canada says it has no legal power to enter into binding agreements with the United States, then I think nothing good will come of this.

So, therefore, Mr. President, it is my intention to support a resolution of disapproval.

The CHAIRMAN. Let me indicate what the situation is. And Jack, I wonder if you might go and vote—we have a vote on right now—and come back. We are going to have four votes this morning, and I am going to try to make sure that we can vote. Do the two of you want to vote and come back, and we will take the opening statements? All right.

We will just run this straight through, and we hope to have somebody presiding all the time.

Senator Symms.

Senator SYMMS. Thank you very much, Mr. Chairman, and I will be as brief as possible so we can expedite and get our two colleagues testifying and the other witnesses that we want to hear from. I must say, Mr. Chairman, that I am most heartened to hear the comments of all of our colleagues, as I am sure Senator Baucus is, from a conversation we had yesterday. The way I count the votes, we have enough votes in this committee right now to pass a motion of disapproval. I share what my colleagues have said. And I don't take that position with any particular joy.

I think that it would be nice to have a wide-open border with our friends in Canada and have a free trade zone. I think philosophically it would be a nice thing to be able to do, and it sounds good. However, we have established the fact that the timber is being subsidized in Canada; livestock is being subsidized in Canada; potatoes are being subsidized in Canada, at the expense of American producers. That is just simply not fair trade.

We had a very fascinating hearing in the Joint Economic Committee about this subject. Basically, we stayed on the subject of timber and established that there were, in fact, subsidies taking place on those Crown timberlands. To add insult to injury, we had a furniture manufacturer from New England testify that they were unable to crack the Canadian retail lumber market for a variety of different kinds of barriers that are put up against furniture that is manufactured in New England, trying to go back into Canada.

So, it really is a one-way street. I think that is why, with 114 billion dollars' worth of trade last year, we suffered a $24 billion trade deficit. Now, I have distributed to many of the members and I would just kind of urge you to look through some of the press from the Canadian newspapers of quotes of not only our administration but of the Canadian leadership—of the Canadian Government—the Prime Minister and the Trade Minister. They are very clearly saying that they expect to go forward with the free trade discussions with a clean launch, and I quote the Prime Minister:

He says, "I refuse to accept the proposition advanced by some in the United States that the softwood lumber issue must be resolved in favor of the United States prior to the talks beginning." This is the Prime Minister speaking.

They simply have not thought that we would hold tough on this issue. I just think that those of us in this committee have an obligation to the producers that we represent from the various States on this committee to use what leverage we have and pass a motion for now of disapproval without prejudice until we can work out and establish the fact that we are, in fact, going to have fair trade between us and the Canadians. I yield back to the floor, Mr. Chairman.

The **CHAIRMAN**. Senator Bentsen.

Senator **BENTSEN**. Thank you very much, Mr. Chairman.

Mr. Chairman, if there ever was a country we ought to be able to have free trade with, it is Canada. We have comparable wage scales, comparable cultures; and we save and we spend with about the same propensity. So, we ought to be able to work it out, if it really is free trade on both sides. That is what I would like to see.

My concern, though, is frankly with the administration because I don't know who is in charge of trade. One day, John Block takes on the French and the European Common Market because they had been dumping wheat flour in Egypt and taking that market away from us. So he decides to reciprocate; and we think finally we are going to get agriculture on the agenda with the European Common Market on GATT negotiations. Then the Defense Department rushes over and says: "You can't do that; you must not upset the Europeans. And we are trying to get the cruise missiles in NATO; we are trying to get Pershing II's."

All of a sudden, the administration backs off; and then the Europeans find out that United States trade policy is formulated on an ad hoc basis. We don't really have a coordinated trade policy. Here's another example. We saw Bill Brock, who I think was an excellent Trade Representative, develop a tough policy to open up the markets of Japan. But the State Department rushes over and says: "You can't do that; you know, Japan votes with us in the United Nations most of the time." [Laughter.]

You really shouldn't upset them. And so, Bill Brock folds his tent and decides to be the Secretary of Labor. [Laughter.]

And I don't blame him. The problem is that trade has been in labor for a long time, as far as the policy of this country goes; and we haven't given birth to much of anything. I guess there is only one other way to do it, and that is to make the Congress part of the process. So, Mr. President—I mean, Mr. Chairman—that is not a good title, either. [Laughter.]

But it really disturbs me. I think we have to send a strong signal to the administration that we ought to have someone fighting for the economic interest of this country, and that that is a primary consideration when we see ourselves, as last year with a $148 billion trade deficit and something comparable to that amount this year.

Soon we'll be able to say to all these other debtor nations of the world: "Move aside, you are pikers; we are the No. 1 debtor of the world." By the end of this decade, we have to start selling more than we import, certainly through the 1990's. There is no way we are going to service the debt we owe to other countries. Today, you see Japan with the biggest surplus of any nation in the world. The short-term securities they own in this country—you know, if they ever start calling them in——

You know the difference—the great difference—in this situation with Japan today and what you saw at the end of World War II, when we were the capital-rich country: those folks in Japan don't plan on this being a Marshal plan. They expect to be paid back. The only way you are going to pay them back is by exporting more than you import; and we have to get a coordinated trade policy in this country to bring that about.

So, that is the way I am leaning on this—to vote for a motion to disapprove.

The **Chairman**. Let me, if I could, interrupt you, Lloyd. I have just received a notice that the majority leader is going to hold us to 15 minutes strictly on the votes, and we have about 3½ minutes left. When Senator Danforth gets back, or if some other Republican comes back first, have them start the meeting. Senator Chafee still has a statement, and we will have two Senators back to speak. We will stand in recess momentarily.

[Whereupon, at 10:06 a.m., the hearing was recessed.]

AFTER RECESS

Senator **Danforth**. Senator Cohen, if you would proceed? I am sorry that everybody has gone to the floor, but we are delighted you are here.

STATEMENT OF HON. WILLIAM S. COHEN, A U.S. SENATOR FROM THE STATE OF MAINE

Senator **Cohen**. Thank you very much, Mr. Chairman, for the opportunity to appear this morning to present testimony on this issue. I have prepared a very moderate and restrained and responsible statement for the record.

The problem is that I don't feel very moderate or restrained or responsible this morning. Since coming to Congress back in 1972, I have witnessed industry after industry in my State being crippled by unfair trading practices, while our own Government has stood by, aloof, indifferent, and even callous to the inequities and to the human suffering involved. In fact, I would go on to say that our Government has been not an advocate on behalf of its own citizens; it has in fact treated them as adversaries, forcing them to jump through expensive and time-consuming and ultimately, in my judgment, illusory hoops.

Now, if, for example, they filed a petition under antidumping provisions of the law and proceeded along that path, ultimately they would be told they were in the right church but the wrong pew. They didn't really belong under the antidumping. They should have filed a petition under countervailing duty. And if they had the money and the perseverence and the legal talent to build a persuasive case that, in fact, their competitors had violated the provisions of our laws, the President ultimately would end up by waiving the countervailing duty because the offending country would say: We are sorry, and we won't do it again.

Now, I would like to give just three examples of why I have come to the conclusion that our trade laws have been a cruel hoax on the American people. Senator Mitchell earlier mentioned the issue of potatoes—brown and white potatoes. In my judgment, the Canadian Government has a program to expand exports to the eastern United States at whatever cost necessary to capture that market. Now, the Maine Potato Council filed antidumping proceedings back in 1982. The Commerce Department found dumping margins of 36 percent. I am not even including the exchange rate monetary value differential of some 30 or 35 cents. I am talking about a margin dumping of 36 percent.

And yet, the ITC could find no causal connection between that 36-percent margin and the injury being suffered by the industry. I am called upon to think that you, as a lawyer, know the doctrine of "race ipso locuter," which Thoreau described as when you find a trout in your milk. It sort of speaks for itself. They could find no causal connection after a 36-percent dumping margin and injury to the industry itself.

And of course, the Canadian response was quite predictable. Imports have increased rather dramatically, causing the complete depression in the price of potatoes, and as Senator Mitchell indicated, a depression within the potato industry itself. It costs between $9 and $10 to produce a 165-pound barrel of potatoes—$9 to $10. It is currently selling on the marketplace at 75 cents.

That is the predicament that the Maine potato producers are finding themselves in today. We will lose, in all probability, at least 300 potato farmers this year as a result—a direct result—of that kind of influx, imports coming in under a subsidized basis; and yet, no injury has been found by our agency.

We passed a $49 billion farm bill. There are no price supports for potatoes. There are no export subsidies. There are no diversion programs, even though Senator Mitchell and I requested some small, very limited diversion program; and none of that available for Maine producers. They have allowed to go into a freefall, and there is no prospect in sight that President Reagan is going to send his Vice President off to Canada to talk about the stability of the marketplace.

We don't need another trade petition in the industry. We need some advocates for fairness, and we don't have them at this time in this administration.

I would like to talk briefly about the lumber and wood products industry. In 1982, that industry filed the largest countervailing duty petition alleging that nearly $2 billion in subsidized Canadian lumber and wood products threatened to decimate the United States industry. At the time that petition was filed, Canadian lumber firms had captured about 30 percent of the United States market. In Maine, it was almost 75 percent of our market, and I think you could probably take judicial notice that most of Maine is forested. We have quite a few timber firms and companies in Maine; and yet, 75 percent of the market is owned and enjoyed by the Canadians. Commerce ruled that while the Canadian Government appeared—appeared—to be assisting its lumber industries, the practice of stumpage was not a significant subsidy.

Now, Mr. Chairman, Canadian lumber is allocated by the Crown, which owns some 94 percent of all the forests; and there is virtually no competitive bidding that occurs by Canadian lumber companies. They obtain their raw materials at a fraction of their true cost.

The third major issue for us is fisheries. Senator Mitchell dwelled upon this at some length. It is the same sad story. The Department of Commerce recently found that the Canadians were providing some 55 subsidy programs to their fishing industry. It is the largest number ever found in any such investigation. My greatest regret is that they refused to find that unemployment transfer payments made by the Canadian Government to their seasonal fishermen and such was not a countervailuable subsidy. I might point out just for the record that, for every $1 contributed by the Canadian fishermen to that unemployment fund, they receive $17 in compensation, compared to the average Canadian citizen who gets about $1.70 back per $1 contributed.

And yet, with a $17 return, they found no countervailable subsidy. Nonetheless, I was pleased to find that they did discover at least 55 different subsidy programs for the fishing industry, and that matter is now before the ITC, and perhaps they will at least measure up and find that the subsidies are contributing to the industry's injury.

Let me just talk about one final example that demonstrates what I consider to be the hollowness and the hypocrisy of our concern for fairness. Last year the Commerce Department found that the Canadians were shipping mislabeled and below grade potatoes into the United States. And it was the Department of Agriculture and the U.S. Customs Service that proposed to reduce the number of entry points into the United States through Maine. We have roughly six points. They proposed to reduce it down to three—three major entry points—and then to beef up the inspection on those three points, because what was taking place were Canadian truck drivers were running up and down the Maine border at those six points with their CB radios, telling all the other drivers where they could cross over without being inspected.

And so, it seemed only logical for the Agriculture Department and the United States Customs Service to recommend reducing the number of entry points and beef up our own inspection, so at least we could ensure our own citizens that the Canadians are complying with our rules and regulations. Immediately after Prime Minister Mulroney met with the President, the Department of Agriculture shelved its own proposed regulations. These were proposed in the Federal Register back in January; and yet, the Secretary of Agriculture met with Senator Mitchell and myself and advised us that they were discontinuing those regulations. They were shelving them because they didn't want to offend the Canadian Government.

In my judgment, no greater dive has been taken by the United States since Mohammed Ali knocked out Sonny Liston in Lewiston, ME, with a phantom punch that was never thrown and never felt. [Laughter.]

The Canadians only have to give us a verbal shove, and we fall flat on our backs in the name of being good neighbors. Well, these heels of ours that have been rounded are causing a $15 billion trading deficit right now; and we are engaged in what I believe to be tantamount to unilateral economic disarmament when it comes to dealing with our trading partners; in this case Canada.

So, I support what you, Senator Danforth, and others have said about the need to go slow, to not give this authority to the administration because, frankly, Congress has abdicated its responsibility in the field of trade; and I share Senator Danforth's fear that we will be presented with a situation 1 or 2 years from now in which we will once again be called upon to reaffirm the integrity of the Presidency of the United States and abdicate our own responsibilities.

Thank you very much.

Senator CHAFEE. A strong letter follows.

The CHAIRMAN. Did you get to make your opening statement?

Senator CHAFEE. I did not.

Senator COHEN. I would love to hear it. [Laughter.]

The CHAIRMAN. Why don't you go ahead, and then we will hear from Senator Wilson.

[The prepared written statement of Senator Cohen follows:]

STATEMENT OF SENATOR WILLIAM S. COHEN

I appreciate this opportunity to present my thoughts on any proposed bilateral negotiations between the United States and Canada regarding a so-called "free trade agreement." Mr. Chairman, I can sum up my position by saying that unless the issue of Canadian subsidization of natural resource industries is adequately addressed, I will vigorously oppose any such free trade agreement.

Since I came to the Senate in 1979, I have watched Maine's potato, lumber and fishing industries sustain life-threatening economic damage as a direct result of unfairly subsidized Canadian imports. In each instance, the response of U.S. trade officials has been callous indifference to the facts at hand. In no instance have our trade laws provided any measurable relief to these beleaguered industries.

In the area of round white potato trade, the Canadian Government has embarked upon a long-term program to expand exports to the eastern United States at whatever cost necessary to capture the market. During the antidumping proceedings filed by the Maine Potato Council in 1982, the U.S. Department of Commerce found dumping margins in excess of 36 percent by Canadian producers. Yet, the International Trade Commission (ITC) could find no correlation between this astounding level of dumping and injury to the Maine potato industry.

The Canadian response to the ITC decision has been entirely predictable. Since that 1983 ITC decision, imports of Canadian round white potatoes have increased dramatically, with the resulting price depression—and depression is the proper word—threatenting the very existence of the Maine potato industry. This year, Maine producers are receiving approximately 75 cents for a 165 pound barrel of potatoes which costs them $9-$10 to produce. Representatives of the industry estimate that as many as 300 Maine potato producers may go bankrupt this year as a result of the price erosion caused by in large part Canadian imports.

Unlike other U.S. agriculture producers, there are no price support, export subsidy or diversion programs propping up the Maine potato industry. Maine growers are entirely on their own, and that's apparently the way this administration wants it.

This industry simply cannot afford another trade relief petition. Therefore, any trade agreement with Canada must, of necessity, provide this embattled industry with some measure of protection.

In the lumber and wood products industry, a similar story can be told. In October, 1982, this industry filed the largest countervailing duty petition to date, alleging that nearly $2 billion in subsidized Canadian lumber and wood products imports threatened to decimate the U.S. market. In Maine, that figure approached 75 percent. Even so, the Commerce Department determined that while the Canadian Government appeared to be assisting its lumber industry, the practice of stumpage was not considered to be a "significant subsidy." Therefore, no countervailing duties could be applied. Not surprisingly, the Canadian Government has continued to subsidize its forest products sector.

U.S. lumber manufacturers must bid competitively for lumber from private lands. However, Canadian lumber is allocated from the Crown which controls some 94 percent of the forests. Further, competitive bidding among manufacturers appears to be virtually nonexistent. Typically, Canadian stumpage contracts are let for 20 years with the option of renewal on a non-competitive basis. Clearly, the ability of Canadian lumber manufacturers to obtain raw materials at a fraction of their true cost confers upon them an unfair competitive advantage. It is surprising to me that the Canadian producers have not realized a larger share of the U.S market than they currently hold.

By all accounts, the lumber market in the United States is mature and competitive—growing slowly from year-to-year. The continued importation of subsidized Canadian softwood lumber has, however, contributed to a tremendous oversupply in the U.S. marketplace. As a result, many sawmills in Maine and across the country are facing bankruptcy as they unsuccessfully attempt to survive the onslaught of cheap, subsidized Canadian lumber.

In the upcoming bilateral trade discussions, our negotiators must find a way to force Canadian manufacturers to pay a fair price for their raw materials—especially for those industries that export to the United States. If the current bilateral talks do not resolve this basic imbalance, then the Congress must act swiftly to bring about a legislative solution.

In the area of fisheries trade, recent events have indicated that our Government's message to Canada should not be "let us look forward to a relationship of unrestricted imports on the basis of free trade." Instead, our Government must make clear to the Canadians that until there is some adjustment of Canadian production policies—to encourage fair competition in the domestic marketplace—continuing opposition from U.S. fishermen to the existing unfair trade practices can be expected.

The Department of Commerce recently found the Canadian Federal and Provincial Governments to be providing some 55 subsidy programs to the Canadian fishing industry—the largest number of countervailable programs ever found in a countervailing duty investigation. While I was deeply disappointed that the Department did not find that the seasonal Government transfer payments directly to self-employed Canadian fishermen constituted a countervailable subsidy, I was pleased that Commerce did find such a large array of subsidy programs. I anticipate that the ITC will make a final injury determination next month which, hopefully, will discourage the Canadian Government from continuing to subsidize this sector of the economy.

In closing, I want to relate a recent occurrence which, I hope, is not a harbinger of this administration's negotiating strategy in the upcoming discussions with Canada.

After working for months with the Department of Agriculture and the U.S. Customs Service to implement a proposal reducing the number of border crossings between Maine and eastern Canada available to Canadian shippers because of the increasing occurrence of the importation of mislabeled and under-grade potatoes, I was recently informed by the Secretary of Agriculture that the proposal would be withdrawn because of the fear of retaliation by the Canadian Government. Keep in mind that this was a proposal which for many months enjoyed the strong support of both the USDA and the U.S. Customs Service. Yet, interestingly, immediately after

Prime Minister Mulroney met with President Reagan last month, the Secretary of Agriculture announces that this carefully thought-out proposal was being shelved because the Canadians might retaliate.

If this is reflective of the attitude of our Government before we even begin these negotiations, then I greatly fear for the health and well-being of all U.S. industries potentially affected by a free trade agreement with Canada. Under such circumstances, I have but one question for our negotiators and for this committee: Why bother?

Senator **Chafee**. Thank you, Mr. Chairman. I am glad to have had the chance to listen to the remarks of both my distinguished colleagues from Maine and others.

Mr. Chairman, I am here to listen to the presentation by our U.S. Trade Representative, Mr. Yeutter, and others. I will first start off by saying that Canada has one of the highest tariff barriers of any industrial nation in the world; and I think there is a lot to be gained by the United States in trying to reduce those tariff barriers. I think that there are several problems that we have to be aware of; namely, the subsidies that the Canadian Government clearly provides for its various industries.

I am particularly familiar with the fishing industry, as Senator Cohen mentioned. That is an industry which is subsidized in a whole series of ways, including the construction of fishing vessels. But these are matters that, I think, should be handled in the negotiations.

Second, I think there is the provincial problem. Most of us are familiar with the powers of the provincial governments, and that the central Government of Canada does not speak for the provinces in a host of areas, including in connection with imports and tariffs. That is something that we have to be concerned with.

Also, I want to point out, Mr. Chairman, that this isn't the last bite we get out of the apple. Should this power of the U.S. Trade Representative, the fast track, not be disapproved—in other words, if he proceeds—then he comes back to this committee with the outline of what he has; and we have a chance to make changes then, which he can go back and negotiate further; and finally, it comes to the floor.

Now, there is a counterargument to that which was presented so ably by many here; namely, that the Ron-Bryan relationship is so strong that the United States will be steamrollered to accept anything that is proposed. I don't quite feel that way myself, Mr. Chairman. The power of this Senate to negotiate agreements or to handle the individual parts of an agreement, I think, is extremely limited. As we pointed out earlier, it has taken us 3 weeks to agree to give away two airports. And the distinguished Senator from Missouri, the chairman of the Trade Subcommittee, mentioned that we are held up. The administration doesn't approve a measure that I very strongly support that is pending on the floor of the Senate; namely, a bill to retaliate against the Japanese in connection with electronic and telecommunications equipment.

Now, there is a bill that I feel strongly about, but it isn't the administration that is holding up that bill. It is the Senate of the United States that is holding up that measure, which to me is an indication now that there may be reasons that aren't clear. Somehow the administration has a hand in this, but I know that the chairman of that subcommittee has tried time and time and time again to get that bill up, which came out of this committee, which I would very strongly support. And I don't know what the count in the committee was, but I suspect it was unanimous. Was it unanimous when we brought it up?

Senator **Danforth**. Yes.

Senator **Chafee**. It was unanimous. So, it is not the administration that is the villain of the piece; it is ourselves. We met the enemy and they are us in this instance.

So, Mr. Chairman, I am prepared to listen. I don't have the heavy tilt—or it is even more than a tilt—it is an——

The **Chairman**. An avalanche.

Senator **Chafee**. It is an avalanche against this measure. I am prepared to listen, and I can see considerable merit that could derive from proceeding on the fast-track method.

The **Chairman**. If you are not willing to go along with us, are you willing to get out of the way of the rocks? [Laughter.]

Senator **Chafee**. I haven't been on the prevailing side of too many votes around here lately, so it won't be a unique experience. [Laughter.]

The **Chairman**. Senator Wilson.

STATEMENT OF HON. PETE WILSON, A U.S. SENATOR FROM THE STATE OF CALIFORNIA

Senator **Wilson**. Thank you very much, Mr. Chairman. I want to thank you and the members of the committee for scheduling this hearing to review the administration's decision in negotiating a free trade agreement with Canada because with any diplomatic effort that has the potential to expand our trading system and to open markets for U.S. businesses, to increase choices for American consumers, Congress has the great responsibility to carefully scrutinize both administration policy and any agreement that might be reached.

Now, as this committee knows, as you have been told by one of your members this morning, Senator Mitchell, our trade with Canada is greater than with any other country. Not only is it 27 percent greater than our trade with Japan, but in terms of the 1984 Province of Ontario trade, that alone amounted to a market for more United States exports than the entire nation of Japan. Despite this level of trade unhappily, last year we suffered a trade deficit with Canada of almost $24 billion; and on a per capita basis, that is five times the deficit that we have experienced even with the Japanese.

Now, all this being said, it may surprise you that I will tell you that we should pursue comprehensive agreements to end all barriers to trade with Canada and with our other trading partners, as long as there is true reciprocity: reciprocity for agricultural and manufactured goods; reciprocity in the treatment of intellectual property; reciprocity in services and reciprocity in investment opportunities. It is not enough, gentlemen, that we seek a free trade agreement that meets the requirements of article 24 of the General Agreement on Tariffs and Trade, for to do so would be to sell short many of our most efficient and competitive industries.

One need only look at the catalog of trade impediments put together by the U.S. Trade Representative, the 1985 National Trade Estimates, to see that we have a number of trade disputes with Canada, which could be left unresolved, totally unresolved, by a GATT compatible free trade agreement. Article 24 is not the answer.

For example, a GATT compatible free trade agreement with Canada could fail to resolve the Canadian theft and rebroadcast without compensation of United States television signals. It could fail to end Canada's new policy to provide freight subsidies for export of certain grains and feeds ingredients. And it could fail to secure national treatment for the U.S. wine exports and other exports, allowing the continuation of this kind of finger-pointing between the central and the provincial governments.

Now, the barriers are just as real whether they are erected by the provincial or the central government; and I really think that dodge is one that we should not let pass.

Furthermore, a GATT compatible agreement with Canada could fail to end the Canadian policy to force divestiture of publishing companies owned by United States corporations, and there is certainly no reciprocity there. It could fail to end the practice of some Canadian industries to incorporate dumped materials in their United States bound goods. And it could fail to provide patent protection for pharmaceuticals.

Mr. Chairman, I have touched on just a few things. I haven't sought to repeat the complaints heard from my colleagues from Maine about potatoes, about timber, about fishing; but Mr. Chairman, we must ensure that a free trade agreement with Canada has more to it than simply the hopeful ring to its name because what I fear is that a bilateral so-called free trade agreement between the United States and Canada may be, in the final analysis, woefully, in fact fatally, underinclusive.

When we were dealing with television in the Senate, I almost offered a resolution as an amendment that would have said that unless we are satisfied that there is ample coverage of all of the many disputes, the many grievances that have been recited this morning in the opening statements by the members of this committee, that we should disapprove the free trade agreement.

Well, I will say that I think we should pursue the free trade agreement; but Mr. Chairman, if we are to see to it that it has more than simply that hopeful ring to its name, then we are going to have to be concerned that this Congress, and specifically this Senate, has ample opportunity to safeguard the legitimate interests of the American farmer, the American manufacturer, the producer of intellectual property rights. In short, we have to see to it that we are not simply handed a fait accompli in which we have little voice and our sole choice a decision as to either vote it up or down.

If these fears prove to be well founded, if a negotiated United States-Canada free trade agreement is underinclusive, what can we in the Senate do to indicate our concerns or to rectify what we perceive to be errors in that agreement? Well, as this committee knows, we cannot delay its passage. We cannot amend it. We cannot seek better understanding or compromise on the floor. We cannot specify even the areas of our disagreement and ask for further negotiations. No. All that we can do—all—is to vote it up or down as presented to us in its entirety.

Mr. Chairman, in considering a free trade agreement, we are hobbled and by our own hand. We are hobbled by laws that we passed after much too little scrutiny, specifically by sections 102 and 151 of the Trade Act of 1974. For unlike the process by which we consider other international agreements, bilateral trade agreements cannot be amended once the President submits them. Fishing rights treaties are amendable. Tax treaties are amendable. Strategic arms agreements are amendable. Copyright conventions are amendable. But trade agreements are not amendable, even bilateral trade agreements about which we have erected a gag rule just 18 months ago.

Now, this is wrong; and before further trade legislation is disposed of by the Senate, I trust we will rectify our mistake. Just to make my position clearer, I do support negotiations designed to achieve free and open trade between the United States and Canada. Furthermore, I trust that Ambassador Yeutter will strive to achieve a truly reciprocal agreement that addresses all of the issues that last year's annual report cataloged, including those that I have noted.

However, I strongly believe that the Senate should have the ability to backstop our trade negotiators if the need arises and to achieve that ability, I believe that the legislative fast-track provision in the Trade Act must be modified. There are too few hours allowed for debate. No amendments are possible. We are virtually precluded from having a meaningful voice, and I would suggest to you that in that are the seeds of real inequity to industries that are now competing against unfair competition. Thank you.

The CHAIRMAN. Any questions of either of the Senators?

Senator MITCHELL. Mr. Chairman, I would simply like to commend Senator Wilson and especially my colleague, Senator Cohen, not only for their statements but for the very forceful activities in this area in which he has been involved on behalf of the fishermen, lumbermen, and farmers of our State.

The CHAIRMAN. Fellows, thank you very much for coming.

We will now take Ambassador Yeutter.

While he is coming forward, I will insert at this place in the record statements by Senator Thurmond and Senator Domenici on this subject.

Senator BAUCUS. Mr. Chairman.

The CHAIRMAN. Senator Baucus.

Senator BAUCUS. In addition, while we are waiting, Senator Pryor was unable to be here this morning, and he has asked me to also express his views that he has very deep concerns about the free trade agreement and very deep concerns about allowing the fast track to continue at this point.

His particular concern is about timber. Arkansas is quite adversely affected by Canadian stumpage, and he is very deeply concerned about this potential free trade agreement.

The CHAIRMAN. Good morning, Mr. Ambassador.

[The prepared written statements of Senators Wilson, Thurmond, and Domenici follow:]

Statement of Hon. Pete Wilson, a Senator From the State of California

PROPOSED UNITED STATES-CANADA FREE TRADE AGREEMENT

Mr. Chairman and members of the Committee, I want to commend you for scheduling this hearing to review the administration's decision to negotiate a free trade agreement with Canada. As with any diplomatic effort that has the potential to expand our free trading system, to open markets for U.S. businesses, and to increase choices for American consumers, the Congress has a great responsibility to carefully scrutinize both administration policy and any agreement that may be reached.

As the Committee knows, our total trade with Canada is greater than our trade with any other country. Not only is our trade with Canada 27% greater than our trade with Japan, but in 1984 the Canadian province of Ontario—on its own—took more U.S. exports than did the entire nation of Japan.

Unfortunately, despite this high level of trade, last year we suffered a trade deficit with Canada of almost $24 billion. On a per capita basis, this is five times the deficit we experienced with Japan.

All this being said, I believe that we should pursue comprehensive agreements to end all barriers to trade—with Canada and others—as long as there is true reciprocity. Reciprocity in the treatment of intellectual property. Reciprocity in services. And reciprocity in investment opportunities.

It is not enough for us to seek a free trade agreement that meets the requirements of Article 24 of GATT, for to do so would be to sell short many of our most efficient and competitive industries. One need only look at the catalogue of trade impediments put together by USTR, the 1985 "National Trade Estimates", to see that we have a number of trade disputes with Canada which could be left unresolved by a GATT-compatible free trade agreement.

For example, a GATT-compatible free trade agreement with Canada could fail to resolve the Canadian theft and rebroadcast, without compensation, of U.S. television signals. It could fail to end Canada's new policy to provide freight subsidies for export of certain grains and feed ingredients. And, it could fail to secure national treatment for U.S. wine exports, allowing the continuation of provincial government barriers.

Furthermore, a GATT-compatible agreement with Canada could fail to end the Canadian policy to force divestiture of publishing companies owned by U.S. corporations. It could fail to end the practice of some Canadian industries to incorporate dumped materials in their U.S.-bound goods. And, it could fail to provide patent protection for pharmaceuticals.

Mr. Chairman, we must ensure that a free trade agreement with Canada has more to it than a hopeful ring to its name, for what I fear is that a bilateral, so-called "free trade agreement" between the U.S. and Canada may be, in the final analysis, woefully underinclusive.

And if these fears prove to be well founded, if a negotiated U.S. Canada free trade agreement is underinclusive, what can we in the Senate do to indicate our concerns? As this Committee knows, we cannot delay its passage. We cannot amend it. We cannot seek better understanding and compromise on the floor. We cannot specify the areas of our disagreement and ask for further negotiation. No. All that we can do is vote it down—as presented and in its entirety.

When considering a trade agreement, we are hobbled—and by our own hand. We are hobbled by laws that we passed after too-little scrutiny—sections 102 and 151 of the Trade Act of 1974. For unlike the process by which we consider other international agreements, bilateral trade agreements cannot be amended once the President submits them.

Fishing rights treaties are amendable. Tax treaties are amendable. Strategic arms agreements are amendable. Copyright conventions are amendable. But trade agreements are not amendable—even bilateral trade agreements, about which we erected a gag rule just 18 months ago.

This is wrong, and before further trade legislation is disposed of by the Senate, I trust we will rectify our mistake.

Just to make my position clear, I support negotiations designed to achieve free and open trade between the U.S. and Canada. Furthermore, I trust that Ambassador Yeutter will strive to achieve a truly reciprocal agreement that addresses all of the issues that last years annual report catalogued—particularly those I have noted. However, I strongly believe that the Senate should have the ability to backstop our trade negotiators if the need arises, and to achieve such an ability, I believe that the legislative "fast track" provision in the Trade Act must be modified.

Thank you.

Statement by Senator Strom Thurmond

Mr. Chairman, I would like to commend you and the other distinguished members of this committee for holding this hearing and it is a pleasure to testify here today.

Mr. Chairman, Canada is our largest trading partner; she is our ally and friend. I have urged the Administration to negotiate a free trade agreement with the Canadians so that we may further open lines of communication and trade between our countries.

Any agreement of this nature, however, must address certain unfair trading practices and the impact of these practices on the timber industry of the United States. Unfortunately, our domestic timber owners, the loggers and others working within the industry, are threatened by subsidized imports of both raw and processed timber from other nations, especially Canada. As you know, Canada has captured over 30% of our domestic market.

According to the International Trade Commission (ITC), in 1984 the cost of lumber in Canada was approximately $10 per thousand board feet. This same ITC report estimated the cost of United States lumber at over $100 per thousand board feet. Mr. Chairman, the relatively low value of Canadian lumber which is the result of direct and indirect Canadian subsidies, combined with the low value of the Canadian dollar are forcing many of our logging operations, sawmills, and lumberyards out of business.

I understand that preliminary talks are currently underway concerning the United States/Canada free trade agreement. I commend Ambassador Yeutter and Secretary Baldrige for addressing this important issue with the Canadians. However, unless the timber trade problem is resolved, the final approval of a free trade agreement by the United States Senate will be seriously jeopardized. It is my hope that a free trade agreement can eventually be reached.

I urge you and other Committee members to keep these points in mind during your consideration of the "fast track" procedure for the United States/Canada free trade agreement.

U.S. Senate,
Committee on the Budget,
Washington, DC, April 11, 1986.

Hon. Robert Packwood,
Chairman, Senate Finance Committee,
Dirksen Building, Washington, DC.

Dear Bob: I want to commend you for holding hearings on the proposed Free Trade Agreement between the U.S. and Canada. Trade between the U.S. and Canada constitutes the largest trading relationship in the world. The numbers dramatize the magnitude and importance of such a free trade agreement. Thirty-one percent of total U.S. imports come from Canada and 21 percent of total U.S. exports go to Canada.

A substantial percentage of this trading relationship is in the mining sector, and it could become more and more important as many of the larger Canadian ore bodies are brought into production.

According to a preliminary study done by the Bureau of Mines, uranium and potash are two U.S. minerals sectors which could experience significant economic dislocations as a result of a free trade agreement.

Approximately two-thirds of the uranium imported into the U.S. comes from Canada. The Canadian government is heavily involved in this industry, owning most of the major producing companies. They exclude all U.S. producers from their markets, and review all export contracts. Each year they set a "floor" price that returns the producers' cost and maintains a level of profit that keeps their industry viable. The Canadian government also pours millions of dollars into the industry in exchange for stock in the producer-companies. Canada then sets the market price in their country at a level four times that of what they will sell uranium for in the U.S. This is undermining the viability of the U.S. uranium industry. Further, the U.S. conversion industry is in danger because of the Canadian government's new requirement that all of its uranium be converted in their facilities as soon as the U.S. contracts expire.

Domestic uranium producers have previously focused their efforts on getting the Department of Energy to exercise its authority under the Atomic Energy Act. However, I think these trade talks could provide the necessary opportunity to address some of these issues if the negotiations are broad enough in scope.

Another significant industry in my state is potash. New Mexico produces 97 percent of the potash produced in the U.S. Canada is the largest potash producer in the world. Presently, there are no Canadian or U.S. tariffs on potash so that unless the Finance Committee insists, it is unlikely that potash would be a topic of trade negotiations.

However, there are a few potash issues that I believe should be resolved before the U.S. enters into a trade agreement with Canada.

The Canadians were found to be dumping in 1969, but the case dragged on and by the time a dumping order was entered into the Canadian companies had not dumped for a substantial period of time. The Commerce Department recognized this "rehabilitation," and in view of it, dumping margins were not set nor tariffs required to give assurances that they would monitor their selling prices and make sure their future sales would not be made at less than fair value. As a part of these assurances a monitoring system was also created. It was stipulated that, if necessary, there would be price action taken to adjust export or home market prices. In reality this mechanism does not exist.

The existence of these assurances, however, creates a presumption that the Canadians are complying with the law, but recent data suggests that some companies are once again dumping. As I understand the situation, if U.S. companies were to bring a dumping action they would have to prove the usual case, and also overcome this presumption of Canadian fair pricing. The presumption exists because the assurances exist.

The Free Trade negotiations could be an excellent opportunity to revitalize the monitoring system. In view of recent pricing practices the monitoring could prove very beneficial.

Another item that should be examined in the context of evaluating whether there should be a free trade agreement is transportation rates and the impact they have on all Canadian exports. I think an inquiry into how transportation rates are arranged in Canada should be considered. It is important for potash, for timber and numerous other commodities.

Another problem that is pervasive throughout the mining sector is overproduction. Canadian potash is a good example. World consumption has been somewhat flat since 1970. However, Canada went from 3.41 million tons in 1970 to 8.54 million tons in 1984 and 7.32 million tons 1985, a compound growth rate of 5 percent. The increase in production was certainly not demand driven. One company owned by Saskatchewan Province controls 43 percent of Canadian production and has a continuing policy of maintaining its market share despite oversupply and falling world prices. This has led to depressed world market conditions and little profit for industry participants.

I really don't know how to best address the problem of surplus production in the context of bilateral trade talks, but I would certainly encourage your Committee to study the problem and make recommendations as to how it should be corrected.

Bob, I want to share with you a letter I wrote to Robert Horton, Director of the Bureau of Mines, requesting a study on the impact a free trade agreement would have on the potash and uranium industry. I would hope that when the study is completed we will have an opportunity to discuss it in the context of the Committee's evaluation of the negotiations.

With warm personal regards,

PETE V. DOMENICI.

U.S. SENATE,
COMMITTEE ON THE BUDGET,
Washington, DC, April 10, 1986.

Mr. ROBERT C. HORN,
Director, Bureau of Mines, Department of the Interior,
E Street, NW, Washington, DC.

DEAR MR. HORN: As a Senator from New Mexico, a state abundant in natural resources, I am particularly concerned about the effects the on-going United States-Canada Free Trade Agreement negotiations may have on mining in general and the potash and uranium industries in particular. Many factors, including international trade flows, are having a significant impact on mining in our country. Reseach which may illuminate aspects of international trade specific to mining is especially timely. I believe we have a common concern for these issues.

In order to examine the potential implications of the United States-Canada Free Trade Agreement, I would like to request a quantitative analysis of the effects any eventual Agreement provisions would have on the United States' mining industry, with specific attention given to potash and uranium. Focussing on comparative costs, natural markets, and transportation inputs should provide a comprehensive view of the impact the Trade Agreement would have on these industries. In addition, I would think that both the mining and processing sectors should be included in the over-all study, but should be analyzed separately.

I had a study in mind similar in scope and depth to the study the Bureau of Mines did on Columbian coal. Such a study should be useful to both negotiators and industry representatives.

Your attention to the expedient formulation and analysis of this information would be greatly appreciated by me and the people of New Mexico that have a stake in the future of these vital industries.

Sincerely yours,

Pete V. Domenici,
U.S. Senator.

STATEMENT OF HON. CLAYTON YEUTTER, U.S. TRADE REPRESENTATIVE, WASHINGTON, DC

Ambassador **Yeutter**. Good morning, Mr. Chairman.

The **Chairman**. Have you had a good morning? [Laughter.]

Ambassador **Yeutter**. It was a lot better before I came here.

Senator **Bentsen**. I wasn't sure he was going to show up. [Laughter.]

The **Chairman**. Go right ahead.

Ambassador **Yeutter**. Thank you, Mr. Chairman. Well, we have before us a very significant issue in the relationships of Canada and the United States, and I must say that the discussion this morning will have major implications in that relationship. I think the Senate Finance Committee will probably make 6-inch headlines in every Canada paper tomorrow morning, and I suspect an awful lot of time and attention on television stations in Canada. Now, what that will lead to in terms of our political and economic relationships, only time will tell; but one should have no misunderstanding about the implications of what has been said here this morning and the reverberations that that will bring about in Canada and perhaps elsewhere in the world as well.

I don't know what the reaction of the Government of Canada will be, if the attitudes that are being expressed here are followed by a vote that would reflect those expressions.

Clearly, the Government of Canada will have to make its own decision as to whether it is prepared to go forward with these negotiations on other than a fast-track basis. Certainly, my opinion would be that the Prime Minister did not have the expectation that fast-track authority would not be provided and that the negotiations would be, in essence, held hostage to that process. But I certainly do not in any way expect to speak for the Prime Minister or for the Government of Canada. It may also have reverberations in terms of relationships with some of our other trading partners in terms of the messages that it sends, and it clearly has implications to the ongoing bilateral disputes in Canada.

I don't know whether this will be helpful or harmful in terms of dealing with existing disputes, some of which were mentioned here this morning—timber and pharmaceuticals and others—but I am sure it will lead to an agonizing reappraisal in Ottawa of the Canadian attitude on these issues, and we will know within a few days what the fallout on that is.

But putting all of that aside, I would really like, Mr. Chairman, to get to the basic question involved and trust that we will not lose sight of the potential benefits to both countries of a true free trade arrangement. President Reagan indicated when he sent this proposal over to the Congress that he felt this provided a historic opportunity for the two countries, and I truly believe that to be true.

In my judgment, this is the single most important trade decision that has been taken in this country probably in this century. I really believe the potential benefits to the United States and to Canada are greater than any other single thing that the two nations could do for many, many decades to come. There is just no question that in economic terms, a free trade arrangement between the two countries could be enormously beneficial to both.

This is not a situation where one country must gain and the other must lose. It is not a zero sum game; it is not a finite pie. We are dealing here with a pie that could expand dramatically as a result of the arrangement and one in which major industries in the United States and Canada and thousands of firms can benefit. So, it seems to me that we need to think very carefully about whether or not we torpedo a process that has that much potential benefit to this country and to business firms of the United States.

I should add in that regard that there has already been a substantial amount of consultation with the private sector in this country on a United States-Canada negotiation, more in this country than in Canada. The Canadian negotiators conceded yesterday that we were much further along in this process than they were. We have 40 to 50 of our advisory committees working on U.S. objectives for this negotiation. They have a May 15 deadline to bring back their recommendations to us as to what our principal economic objectives in the negotiation should be.

There has been a strong endorsement of this process by our advisory committee on trade negotiations, which is the Presidential level committee that has representatives from most of the major industries of this country. Additional support has come from a whole host of business organizations, including the National Association of Manufacturers, the U.S. Chamber of Commerce, ECAT, the National Foreign Trade Council, and others. That is a lot of high-powered support for the concept of moving forward with a United States-Canada free trade arrangement.

In terms of benefits, it seems to me that the economies of scale should be evident and of very substantial benefit to both nations if an exercise like this were implemented. In terms of the basic prospects that were involved for American firms——

The CHAIRMAN. Let me interrupt you just a moment.

Ambassador YEUTTER. Yes.

The CHAIRMAN. We have another vote. Senator Danforth has gone, and I will wait here until he comes back; but the members should be alerted that we do have a vote, and Senator Dole says he is going to hold very tightly to the 15-minute limit. Go right ahead.

Ambassador YEUTTER. OK. In terms of opportunities for American business firms, it just seems to me that anything we can do to smooth the access of American firms to Canadian resources and to the Candian market, that would be enormously beneficial. The fact is that, as friendly as the relations are between our countries and as comparable as our economies are, it is not as easy to do business between Minneapolis and Winnepeg as it is to do business between Minneapolis and St. Louis. And if we can essentially eliminate the borders between the United States and Canada to international trade, maybe it will be just as easy to do business between Minneapolis and Winnepeg as it is between Minneapolis and St. Louis. And it seems to me that an awful lot of American businesses throughout the country, not just along the border between the United States and Canada, can benefit from that exercise.

In terms of comments that I heard earlier that we are not as well staffed for this exercise as Canada, that may be true at the moment because Peter Murphy, who will be our chief negotiator, has just returned from Geneva, Switzerland. As you know, Peter has been our representative at the General Agreement on Tariffs and Trade in the last several years He had been our chief textile negotiator prior to that. And Peter is just in the process now of putting together the team that will handle these negotiations.

Peter and I met with Mr. Reisman, the chief Canadian negotiator, yesterday; and certainly we are impressed with the preparations that Canada has engaged in thus far, but we are certainly not prepared to concede that we are going to be out-negotiated by the Government of Canada on this issue. I don't happen to think we will be, and I happen to think that we will have as many or more human resources and just as much or more talent devoted to this exercise as it gets underway than the Government of Canada will have.

We have a small number of people from the USTR that will be involved in this process, but that is always the case. The whole intent is to bring people intn the exercise from other critical and key agencies of Government that have an interest. Peter has the responsibility of assembling that team. I am confident he will assemble a very effective team that will represent the interests of the United States in a very effective way in the negotiations.

So, if there be concerns about whether or not we are going to give away the store, Mr. Chairman, we have no intention of giving away the store. And I can't speak for years past, but I don't think we have given away the store on anything since last July 1, when I came back into Government. That may be a self-serving comment, but I am prepared to have that appraised objectively by anybody.

So, we don't intend to abandon our negotiation skills or in any way reduce them for this exercise as compared to any other exercise.

In terms of specific interests and benefits that we may achieve in this negotiation, clearly—and this is in response to the comment that, gee, we have given everything; how are we going to reach an agreement that would be beneficial to the United States—well, that is a question of negotiating skills, of course. But I will say what we would like to achieve.

In terms of the tariff area, everyone here knows full well that Canadian tariffs are substantially higher than ours. So, to the extent that we can reduce the tariff differential between Canada and the United States, that obviously will be a net benefit to the United States. Average tariff levels in Canada are somewhere in the 9- to 10-percent range; ours are in the 4- to 5-percent range. We have a very substantial number of requests on our desks today from American businesses and industries to try to reduce tariff levels in this negotiation. I am sure we have had 50 or more letters from companies in the furniture industry alone that have expressed a strong interest in this. The same applies to telecommunications, home appliances, electronics, boats, aluminum products, and a whole host of others. There is a very strong interest in Canadian tariffs.

On the nontariff measure side, of course a lot of the concern is with provincial nontariff measures as well as those at the Federal level, and clearly we have to be able to reach those in the negotiating process. Many of these apply to government procurement practices that are being followed by Canadian provinces and by the Canadian Federal Government.

Again, two major areas of interest to some of you individually would be telecommunications and power-generating equipment. Also, a great deal of interest in alcoholic beverages because our industry in that arena feels that it has a lot of potential in Canada and is being severely discriminated against by many of the provincial governments in particular.

And then, of course, our agricultural community has a lot of interest in this negotiation as well, particularly in specialty crops areas that are represented by Senator Wilson, who was here just a few minutes ago, and others because of the market potential of those products in Canada.

Aside from the goods area, we also think that there is a lot of potential benefit to the United States here in services. And in fact, our hope has been, if we engage in this negotiation, that what we might develop in the way of rules on services could be a model for use in the multilateral trade negotiations in Geneva. We think the United States has a lot of potential to move forward in services.

Senator HEINZ. Mr. Ambassador.

Ambassador YEUTTER. Yes, John.

Senator HEINZ. With your permission, could I just interrupt you to make a comment?

Ambassador YEUTTER. Sure.

Senator HEINZ. In a sense, it is out of order, but we have five bells, and I then have to catch a plane, I am sorry to say. Let me, if I may, Mr. Chairman, just proceed for about 60 seconds; if you have to go and vote, I will recess the hearing if you want me to.

The CHAIRMAN. I think Senator Danforth will be back.

Senator HEINZ. Very well. First, I have no objection in principle to the idea of a free trade relationship between the United States and Canada, even though I am aware that any time we do have bilateral trade agreements, there is the potential for undercutting the MFN principle of the GATT. And there is a philosophical argument against such relationships.

In saying that the principle, on balance, doesn't concern me, however, I would not want anyone to get the idea that there are not some very deep, significant problems that I see. I have mentioned a number of them to you; and my colleagues, I know, have emphasized, for example, the problem of the Canadian Government's relationship to its provinces.

Ambassador YEUTTER. Yes.

Senator **Heinz**. And I don't think that can be underestimated as a difficulty because, no matter what kind of agreement you get with the Canadian Government, it is almost inconceivable to most of us how any such agreement could permanently—and I emphasize the word "permanently"—bind the provinces.

There may be a way, but we don't know what it is; we can't see what it is. And we would need to be convinced that there was a mechanism. There are sectoral issues, but those concern me less than the broader kinds of difficult, thorny problems. A general issue—and you just touched on it in your remarks—is that we have done a pretty good job in negotiating down our tariff barriers. We have reduced our tariffs to the point of zero in many cases.

The Canadians start from a much higher level of tariffs and a wider range of protection. And while it is true we have a lot to be gained if they come down, it is also true that in terms of bargaining dynamics, they start out in a much better position because usually bargaining implies reciprocity; and if they are going to give an advantage of 50 percent to us in terms of the way they cut their tariffs, they are going to look for a similar concession to them. Since they start out in a preferred position, I think it is very difficult to overstate your challenge and difficulty from the position you start in.

And finally, I just want to particularly emphasize the point that a trade liberalization measure with Canada, assuming that we can solve these problems and hopefully you can—I don't think it will be easy—cannot be divorced from the overall issue of how we go about dealing with trade problems generally in the world. Trade liberalization with Canada can't be divorced, for example, from the efforts that many of us think have to be made to do a better job of regularizing the enforcement against unfair trade practices against the United States.

To put it in more stark political terms, it is going to be difficult, if not impossible, for members of this committee to vote for a trade liberalization measure with Canada if we don't stick up for the United States more where other countries are concerned, because people will say to us, look, you fellows told us that in 1979 when you voted for the Trade Agreement Act of 1979; look how well that has worked, they can say. You know, the trade deficit was tiny back in 1979. Now, it is huge. We have lost a lot of manufacturing jobs that don't tell us that trade liberalization is going to help us, they will say, unless you have something to show what you have done to correct some of the, perhaps, errors that were made in 1979.

So, I just want to emphasize that very important point here. For there to be, I think, a realistic hope of progress in this area, it will have to be linked with progress in those other areas, and that is going to require congressional legislation on something more than just Canada.

I thank you for yielding, and I am deeply grateful to you for yielding me that time. And I am going to be very rude and leave and vote. And I apologize to you.

Ambassador **Yeutter**. Thank you, Senator Heinz.

Senator **Long**. Let me make just one statement. Let me just interrupt one second here.

Ambassador **Yeutter**. Sure.

Senator **Long**. I am not going to leave. The Senate is voting; I will just miss the vote. The question is on a motion to table; if the motion fails, I will go over there and vote with the guy who made the motion on the next go-round. [Laughter.]

Senator **Long**. Sometimes, if you are going to get on with the work, you just have to miss a vote or two around this thing. I have done it before; like I said, it is just one of those things. [Laughter.]

Ambassador **Yeutter**. It sounds like a man who is not at all fearful about reelection. [Laughter.]

Senator **Long**. I didn't know you knew. [Laughter.]

Anyway, I am going to stick with you, Mr. Ambassador. So, you go right ahead.

Ambassador **Yeutter**. OK. Thanks, Mr. Chairman.

Let me just make three or four additional comments for the record, and then we can proceed with some questions.

I was focusing, as you know, Senator Long, on some of our major objectives, and I indicated that the services area would be one that we would really like to make some progress in because there is a lot of interest, and we feel a lot of potential in a whole host of services areas. The other one is the investment area, trade-related investment kinds of issues, where as you know the United States has been displeased with a number of Canadian practices in the whole investment arena; and we would like to be able to focus on some of these in this negotiation.

And also, as you additionally know, we have been displeased with some of Canada's actions in the intellectual property arena. We believe that the Canadians ouught to set a better example for the world in the way they handle issues like patents—the recent pharmaceutical patent dispute—although that one hopefully will be resolved well ahead of these negotiations. It illustrates concerns that we would like to deal with in this negotiation with the Government of Canada over the next 2 or 3 years. So, all in all, when one adds together tariffs and nontariff measures and investment services and intellectual property issues, that is a very substantial and significant package of interest to the United States. Clearly, the Government of Canada is going to have some of its own interests. As Senator Heinz indicated, it takes two to tango; and clearly, they will expect some concessions from us, and it might be worthwhile to indicate what we perceive to be some of their major objectives.

One, again, would be tariffs, even though our tariffs are very low on the average; we have some selective tariffs that are relatively high and of concern to the Canadians. And I suspect they are going to want to talk about those. We also have a number of "Buy American" provisions, a good many of them at the State level. So, not only are we concerned about the provinces, as Senator Heinz indicated, they are also concerned about what we do at the State level and what we do at the Federal level, too, to some degree, with "Buy American" laws.

And as I believe Senator Heinz indicated, there is some feeling in Canada that we administer our trade remedy laws in a manner that is unfair to them. We don't happen to share that judgment, but obviously, we are prepared to listen to any arguments that they would like to make on that score and will do so. And we will defend our own laws vigorously in that respect, but we ought to be prepared to listen.

All in all then, Mr. Chairman, Senator Long, the conclusions I would come to are that there is a lot of potential to the United States in this kind of an agreement, and I am convinced that over the next couple of years we can negotiate an arrangement that would be very favorable both to Canada and to the United States.

[The prepared written statement of Ambassador Yeutter follows:]

Testimony of Ambassador Clayton Yeutter
United States Trade Representative
Before the
Senate Finance Committee
on U.S.-Canada Trade Negotiations
April 11, 1986

I want to thank the Committee this morning for the opportunity to appear before you today to discuss U.S.-Canadian trade relations and in particular the proposal from Canadian Prime Minister Mulroney for comprehensive trade negotiations between the United States and Canada.

Trade between the United States and Canada is all too often taken for granted. Our trade problems with Japan and the European Community are so much in the spotlight that most Americans do not realize Canada is our largest trading partner. Yet the roughly $120 billion dollar trading relationship between Canada and the United States is the largest of any two nations in the world.

We are each others' major export market. U.S. exports to Canada last year accounted for around 22% of our total exports, while over 75% of total Canadian exports were to the United States. Perhaps even more importantly, from the U.S. perspective, is the fact that U.S. exports to Canada are growing. In 1985, our exports to Canada increased by 2%. This contrasts with the decline in exports to the European Community of 2% and a decline in exports to Japan of 4% during the same period.

On September 26, 1985, Prime Minister Mulroney proposed bilateral trade negotiations between the United States and Canada on the "broadest possible package of mutually-beneficial reductions in barriers to trade in goods and services." We have welcomed the Prime Minister's proposal for trade talks as fully consistent with the efforts of both the Administration and the Congress to open foreign markets for U.S. exporters. Therefore, on December 10, 1985, the President formally notified this Committee, as well as the Ways and Means Committee in the House of Representatives, of the Administration's interest in entering such negotiations.

Since the proposal by the Prime Minister was made public in September, we have held extensive consultations with our private sector advisory committees to elicit their reaction to the proposal. As the Members of the Finance Committee are well aware, we have a formal advisory system comprised of 44 separate, private sector advisory committees which represent industry, labor and agriculture. We have briefed each of these Committees on the proposal from the Canadian Government, and I can report that there is generally broad support for entering negotiations with the Canadian Government. In fact, the President's blue-ribbon Advisory Committee for Trade Negotiations has examined the proposal from the Prime Minister and has formally endorsed the proposed negotiations. In addition, a number of major trade associations have also gone on record in support of broad trade negotiations with Canada. These include the National Association of Manufacturers, the U.S. Chamber of Commerce, the Emergency Committee for Action on Trade, and the National Foreign Trade Council.

In our discussions with the private sector, we have identified six broad areas of interest which they would like us to pursue in these negotiations. I would like to take a moment to describe each of these areas and some of the industries which have expressed particular interest in them.

One of the most frequently mentioned problems for U.S. exporters seeking access to the Canadian market is high Canadian tariffs. Canadian tariffs average between 9 and 10 percent as compared to U.S. tariff levels which average around 4-5 percent. Among those U.S. industries most interested in seeing high Canadian tariffs eliminated are furniture, telecommunications equipment, home appliances, cosmetics, electronics, paper products, recreational boats, aluminum products, wallcoverings and leather.

The second broad area of concern expressed by U.S. industry are nontariff barriers maintained at both the federal and provincial level. When one studies the Canadian market one becomes quite aware that under their constitutional system significant nontariff barriers can be maintained by the provincial governments. Therefore, it is imperative, from a negotiating perspective, that we pursue reduction and elimination of nontariff barriers maintained both by the national and provincial governments. In particular, we have heard complaints about government procurement preferences maintained by both the federal and provincial governments which favor domestic manufacturers over imports. The telecommunications equipment and the power generating equipment industries are particularly disadvantaged in this regard.

In addition, the U.S. alcoholic beverage sector faces significant discrimination at the provincial level due to discriminatory mark-ups, listing practices, and distribution systems. Both U.S. beer and wine interests have expressed concern over the discrimination they face in entering the Canadian market, and have expressed support for addressing these concerns in any negotiations. A number of other nontariff barriers also exist in Canada which limit exports from the United States of poultry, eggs, dairy products and meat. Technical standards are also used at times as nontariff barriers to the detriment of U.S. agricultural and plywood interests.

A third area which is a point of contention in U.S.-Canadian relations is the treatment of foreign investment in Canada. Under the Government of Prime Minister Mulroney a significant liberalization has taken place in the Canadian investment climate in Canada. However, some outstanding problems for U.S. policy and U.S. business still remain. We would like to see all of these particular issues as well as questions of general Canadian direct investment policy negotiated to a successful conclusion. Our objective is to produce a Canadian policy enviornment as open to inflows of foreign direct investment as in our own.

The fourth area of interest to the U.S. private sector is trade in services. There are a number of service trade areas where we would like to see trade facilitated. Of particular interest will be transportation services including trucking, information and computer services, insurance, professional services and advertising. We have an excellent opportunity to develop rules to govern trade in services in a bilateral context with Canada which could conceivably be a model for the multilateral negotiations in Geneva.

A fifth area of concern to the U.S. business community is the protection of intellectual property. This is also a key objective of the Administration in both the upcoming GATT negotiations and on a number of bilateral fronts. Fortunately, our concerns with Canada in this area are fairly limited although very important. We have longstanding concerns regarding inadequate protection in Canada of pharmaceutical patents, as well as the absence of copyright protection of U.S. broadcasting which is picked up and retransmitted throughout Canada. It is clearly the intention of this Administration to secure intellectual property protection in both of these areas, hopefully before the comprehensive bilateral negotiations even begin.

The sixth area which has been highlighted to us by both a number or U.S. industries and Members of Congress is the question of various forms of government assistance in Canada both at the federal and provincial level. If we are speaking of free trade, these areas need to be addressed.

For their part, the Canadian Government has expressed interest in securing and enhancing access to the U.S. market. While we have not yet had detailed discussions on their specific objectives I will attempt to discuss what I believe to be some of them.

The Canadians wish to have U.S. tariffs reduced or eliminated in the context of a bilateral trade agreement. Even though, as I noted earlier, our tariffs average only around 3-4 percent, we do maintain fairly high tariffs on a select number of products.

On the nontariff barrier side, a major Canadian objective will be our "Buy America" provisions at both the federal and state levels. This is a longstanding interest of the Canadian Government and I would imagine that they will seek a bilateral accord which will liberalize these provisions for Canadian firms.

Another area which we expect the Canadians to pursue is our

U.S. trade remedy laws. There is a perception in Canada that our countervailing duty and antidumping laws unfairly harass import competition. While I disagree with this view, the Canadians clearly believe they should be entitled to a more predictable market in the United States.

Another major area of interest to the Canadian Government is bilateral dispute settlement. The Canadians will wish to have an institutional mechanism in place at the end of the negotiations to enforce any agreement which may emerge from these negotiations, and to deal with individual disputes which inevitably arise between major trading countries.

After listening to this potpourri of issues which are likely to be surfaced by the two sides, I trust you will agree with me that this will be a very difficult negotiation. Nevertheless, if successful, it will be worth the effort for the outcome could enhance prosperity for both countries in a spectacular way.

As an indication of the seriousness we attach to these negotiations, the President has announced that Ambassador Peter Murphy will serve as special negotiator for U.S.-Canada trade, heading the U.S. negotiating team. Ambassador Murphy is a talented and experienced negotiator who has just returned from a very productive tour of duty in Geneva, Switzerland. He will devote considerable time and energy to this endeavor to ensure that your views and the views of the private sector are taken into account.

From my standpoint, I will not present you a negotiating package unless I am confident it is in the long term best interest of the United States.

During these negotiations we will, of course, vigorously pursue resolution of specific bilateral problems and disputes, some of which this Committee is intimately familiar with. I'm aware that some members of this Committee are concerned about the pending trade dispute with Canada over lumber and have suggested that negotiations be delayed until those matters are resolved. I firmly believe, however, that we should not delay. We must not permit individual short-term problems, important as they may be, to obstruct the improvement of our long-term trade relationship, an issue which will be of immense significance in the coming decades.

As you know, we have been engaged in intensive bilateral talks over all elements of the lumber dispute. A senior-level U.S. delegation is today meeting in Ottawa on this problem. It is imperative that we resolve this issue quickly, and this Administration will spare no effort to accomplish that.

We view the proposal from the Prime Minister for comprehensive trade negotiations as a historic opportunity to significantly enhance our trade and economic well being and also demonstrate to the rest of our trading partners the benefit of dismantling trade barriers.

I thank the Committee for your attention and I will be pleased to answer any questions you may have.

Senator **Long**. Mr. Secretary, as far as I am concerned, your job is a Cabinet-level job. If it wasn't for Russell Long, it wouldn't be that way, and I am proud that you are a Cabinet-level man. Frankly, I am proud I fought to make it that way. I fought for it, even with the President not wanting it, and the reason I did was because I thought that, for a person to exercise the responsibility you exercise, you ought to be a Cabinet-level man. Without that, we couldn't have gotten some of the top-notch people who have served in that job. We couldn't have gotten Secretary Dent to leave as Secretary of Commerce and take that job you have.

We couldn't have gotten Bob Strauss to take the job. I doubt if you would have taken the job, minus that.

Ambassador **Yeutter**. No way.

Senator **Long**. We couldn't have gotten Bill Brock——

Ambassador **Yeutter**. This morning, I may not want it, even as a Cabinet position. [Laughter.]

Senator **Long**. But I know a little about hierarchy in the executive branch, and that is why if we are going to be able to rely upon a man, he ought to have the dignity of being a Cabinet-level appointment. I am all for it, even though you don't have the bureaucracy to back you up that these other fellows have who are in the Cabinet.

Now, I want to get a couple of things straight here. You know ordinarily when you say free trade, that just means no tariffs, no limitations, no quotas. Although we call this a free trade agreement, that is not what this agreement is going to be, is it?

Ambassador **Yeutter**. We would like to have it, Senator Long, and get as close to that as we possibly can.

Senator **Long**. But it is not going to be that. You are talking about reducing tariffs; you don't talk about eliminating all tariffs, do you?

Ambassador **Yeutter**. Oh, yes. Oh, yes. We may not achieve that, but we would certainly try to. We did that in the United States-Israel free trade arrangement.

Senator **Long**. But is it realistic to think that when this agreement comes back in, there will be no tariffs whatever with Canada?

Ambassador **Yeutter**. I believe that is realistic.

Senator **Long**. No quotas and no limitations on imports whatever?

Ambassador **Yeutter**. We would like to come—Obviously, one may not get 100 percent, but I would like to get very close to that. The United States-Israeli agreement, Senator Long, comes very, very close to that, if not there; and we would like to do the same thing in Canada.

Senator **Long**. I know about the Israeli agreement. I voted for it because I thought that we could let the Israelis have all the advantages on God's green earth; it wasn't going to hurt us very much because that is a small country.

Canada only has three times the population of Israel, but there is a big difference. In the area of natural resources, they have more land area than we have. I see you are nodding; you know it to be true. And if we have an agreement that is a good deal for one country but not the other, they could just absolutely stomp us in competition, so we need the kind of deal that I would like to see us have. In the oil and gas area, our interests should be really to have a common market with Canada, if we are playing by the same rules.

But if it is like in football where under Canadian rules they have 12 men out there on that football field and under our rules we have only 11, that 12th man will kill you. You can't compete with that. Now, when you negotiate on natural resources, is it not true that they can't make a deal unless they have the acquiescence of those provincial governments?

Ambassador **Yeutter**. Yes. That is true.

Senator **Long**. Now, furthermore—if I am talking out of school, you can correct me, but I think we know this—the only way they can get those Canadian provincial governments to agree, if they are not going to be at that table negotiating, is that those governments are going to have to be persuaded to go along with what is agreed to. Otherwise, they are just not going to give up their right to represent themselves. Isn't that right?

Ambassador **Yeutter**. I would say that is generally right.

They have worked it out in the past, Senator Long. So, I hope they can work it out this time, too. As you know, Canada has been a participant in the multilateral negotiations in Geneva for quite a number of years and they handled the federal/provincial relationship in that context. So, I would assume they will be able to work it out in this context, too.

Senator **Long**. Let me just put it this way: If the shoe were on the other foot, if a trade agreement required the acquiescence of 50 States in order for an agreement to go into effect—a new one to negotiate access for all that gas—and I was the Governor of Texas or the Governor of Louisiana, I would tell you this, Mr. Yeutter. I would say: "If I am not going to be at that table and you are going to represent me, I would be willing to let you bind me on one condition: That you don't agree to anything in this without coming back and discussing it with me and gaining my consent." Isn't that right? You would certainly anticipate that.

I would think that any one of those fellows who ran those provincial governments would be idiots to give up their right to represent themselves unless they have got an agreement with this fellow sitting in there that he is going to clear it with them. So, that is not unprecedented.

When Bob Strauss went over there and negotiated that big agreement for Carter, he had to come back here and clear it with these Senators, both on the committee and people who were going to have to vote on it on the floor. They certainly didn't have a veto, but they did have an opportunity to be considered and to make their views felt and to be satisfied. Now, I think that it is fair that those of us who represent the States of this Union have a right to see that we know just a great deal more about what is likely to come in here.

Just take the natural resources industries. They have a right to know a lot more about what is likely to be imported from Canada before we agree to a fast track. Now, I am not sure that you could even get the right deal on natural resources unless you do some things that haven't been done up until now.

I didn't urge you to do some of those things. I see you are nodding; you know what I am talking about. You are going to have to play a stronger hand, and I am not sure that the administration will let you play the strong hand you ought to play in order to get the deal you ought to get from Canada because right now they are getting all the best of it.

Unless we take a stronger stand than we are right now, we don't have much to negotiate from. That is why we want to know more about what we are likely to get. I can understand why they would like to see this thing going on a fast track basis because, from that point forward, the potential of each individual Senator to defend his interests is a great deal less than it was before that.

I have always been concerned also, Mr. Yeutter, about the fact, as indicated by Senator Bentsen, that if you don't watch out over at the State Department, those fellows won't support you too well. It is all foreign policy; and the Secretary of State and the State Department ought to be able to have the last say about something involving foreign policy. I think that sometimes we have had to tell the State Department that we are just not going to listen to them. We are not going to do it their way.

We want a commercial deal to be free of those votes in the United Nations. That is why I am concerned that we need to have a lot better understanding of what this thing is going to be when it comes back in.

Ambassador YEUTTER. Senator Long, in that respect, all I would say is that it is impossible to lay out everything that is going to happen in the negotiations at this early stage. This is going to be a very complex exercise involving thousands of products and hundreds of industries; and it is an immense undertaking. So, we can be as specific as I was this morning in terms of what our objectives are and where we would like to end up at the end of the day; but to go into enormous detail, it is going to be very difficult because a lot of that depends on what happens at the negotiating table.

You know, we have to have hours and hours and hours of discussions and negotiations before we are really going to know what the end product is going to look like. So, all I can really assure you is that the end product is going to look good as far as I am concerned; or I am not going to bring it back to you.

Senator LONG. But when we did business on the Kennedy round and also in the Tokyo round, you look at the understandings we had with that man negotiating that agreement for us. We had a lot more potential to protect our interests than we see at this moment; and those were much broader agreements than what we are talking about here.

For example in the Tokyo round, Bob Strauss first had to go out and make one deal and then another to satisfy the textile people, on the one hand, and some other group, on the other. So, by the time he got through, he in good faith carried through his commitments, and we felt, "all right, we will go out there and do our part for him."

I just feel that we ought to have the same type confidence that in this case we are going to bring as good a proposal in here as we had under those conditions.

Ambassador **Yeutter**. Sure. Of course, you did use fast track procedures on the Tokyo round, and appropriately so in my judgment. And it seems to me that we ought to use fast track procedures here as well for the same reasons.

Senator **Long**. I am going to have to vote against a fast track, Mr. Yeutter. I want the kind of thing you are seeking, but I want to see that it is a good deal for the United States; and particularly, I also want to represent the State that sent me here. I think the others feel the same way. Frankly, I don't think you can drive as good a bargain as you can make, the minute those people are sure that we are no longer in the picture.

It seems to me that they have got to get this thing at least by the Senate committee, and we need to be looking at something so we can say, "yes, we think it is something that we would be able to live with," before we give it the go ahead on the fast track. Now, please understand that I would like to see a common market with Canada, in everything, but only provided it is a good deal both ways.

Ambassador **Yeutter**. I am convinced, Senator Long, that it can be a tremendous deal both ways. I really truly believe as an economist that this could well be the best thing that has happened to these two countries in decades.

Senator **Long**. If I were as confident that you could make that deal as you are, I would be voting the way you want me to vote. I am not that confident right now.

Ambassador **Yeutter**. OK.

Senator **Danforth**. Senator Packwood?

The **Chairman**. Mr. Ambassador, as you are well aware, from time to time I have talked with you about the lumber issue and told you that there is a fight brewing, not just involving lumber but a number of other industries; and I think you have seen that today.

But let me tell you what the frustration is. Several weeks ago, I am at a social function with the Canadian Ambassador. He talks with me about this, and I said: Mr. Ambassador, of course you mean free trade between the nations? Absolutely. And free investment between the nations? Well, I am not so sure about that.

Of course they want free trade. We have got 250 million people; they have 20 million. If we sell everything we could sell in Canada, it is only a market of 20 million people. So, we would like to invest. Well, they are not so sure they want this. Then what happens? The

Prime Minister goes back, talks to the Parliament on March 21, says we are going to take a bigger piece of the market if we can get it.

Prime Minister Bryan Mulroney on Wednesday slapped the wrists of American Congressmen who were threatening to scuttle free trade talks unless a knotty lumber dispute is settled first. That is fine. That is their Prime Minister. I understand. What is our negotiator saying? Merkin predicted that Congress will give approval this month for a clean launch of talks, meaning Canada will not have to rein in its softwood lumber exports to the United States as a precondition. You know, that is what our defender is saying.

No wonder we have some misgivings about who is representing us, and I don't mean this personally; but we have been frustrated and frustrated and frustrated in trying to get decent responses, and we get the feeling we are being set up as a patsy. And if the Congress will just send out occasional signals that we don't like it, but don't do anything; or send out bills from this committee, but don't bring them up on the floor—why, then, don't worry; the United States will roll over.

As you could tell from the meeting this morning prior to their hearing, we are not going to roll over on this. This is not meant in any way to stick a finger in your eye or to embarrass the President; but the committee has reached the end of its patience. And for a year and a half, we have been trying to get some satisfactory resolution of the Canadian subsidized timber industry problem and the Canadian subsidized potato industry problem and the onion industry and uranium industry problem; and we haven't gotten it. You indicated that the Canadian tariffs are higher than those in the United States. Clearly, they are. They have to be higher to protect subsidized industries that would not be able to compete possibly on a free trade basis.

So, I am going to vote next week to disapprove this resolution, as I think a fair portion or a majority of this committee is going to do so unless I misjudge its sentiment. I don't know what you can do between now and then to convince Senator Mitchell, Senator Baucus, Senator Long, and the others here that somehow a magic wand has been waved in 5 or 6 days, and the attitude not only of the Canadian Prime Minister and Parliament has been changed, but our own negotiator who, in essence, says: Tut, tut, don't worry, folks; they are not serious about it. You don't have to give up any of this softwood timber subsidy. Once we get this thing launched, don't worry about a thing. We will take care of timber; we probably won't even bring it into the agreements.

That does not bode well for the credibility of American negotiators. The best thing we can do for you, Mr. Ambassador, is to turn this resolution down, and you can go back to the Canadians and say: Folks, I told you so. You didn't believe me when you came down there. You didn't believe me when you talked to Senator Packwood. You didn't believe me when you talked to Senator Symms. Well, they are serious. And I hope this gives you some clout to go back to the Canadians and say: Folks, this deal is all over for the next decade unless you start to loosen up and give some good faith signals now. That is the end of my question, Mr. Chairman. [Laughter.]

Senator **Danforth**. Senator Mitchell.

Ambassador **Yeutter**. If I may, I would like to respond to that, in at least a couple of respects. One, with respect to Mr. Merkin's comments. It is always a bit dangerous to assume that what is printed in a newspaper is an accurate reflection of one's statements and attitudes; and I haven't asked Mr. Merkin about those comments, but suffice it to say that he is one of the finest negotiators the United States has ever had.

The **Chairman**. Let me respond to that because all of us have been in politics a long period of time. It is my unfortunate experience to discover that I am seldom misquoted by the press. I am usually quoted accurately on things I wish I hadn't said, but there is a big difference. [Laughter.]

Ambassador **Yeutter**. Well, I know, Senator Packwood, that Bill Merkin is committed to this cause and thoroughly so—and he can speak for himself if need be—but he is not a man that I want off my team; he is a man I want on my team.

Now, with respect to the general issue of the problems that exist, Mr. Chairman, obviously one of the reasons we have negotiations is to try to deal with some of those. We think the lumber situation is coming closer to a conclusion; and in fact, as you know, Ambassador Woods is in Ottawa right now negotiating on that issue today. We were making progress until this morning; I am not so sure about now. But time will provide the answer to that as well.

But in terms of the other issues that you articulated, some of those are clearly issues appropriate for this negotiation, if we have it; and if we don't have the negotiation, it will be more difficult to confront some of those issues, and we will have to try to do them bilaterally in a different setting. But one of the benefits of a broad, comprehensive negotiation like this is that one can make tradeoffs between and among different areas.

That is the same rationale of having a multilateral trade negotiation, and in a way we would hope that the overall package that then emerges, as Senator Long was alluding to, is one that will work out very well, and there will be some winners and some losers, of course, but the intent here is that the result would be phased in over a period of 10 or 12 years. And we are really talking about having the United States and Canada postured then at the turn of the century to move forward with what is essentially a free and open border, which in my judgment would be a magnificent achievement if we can pull it off.

Senator **Danforth**. Senator Mitchell.

Senator **Mitchell**. Thank you, Mr. Chairman. Mr. Ambassador, on February 17 the provincial government of Prince Edward Island announced a $6 million diversion program for its potato farmers. To your knowledge, was any member of the U.S. Government contacted in advance by that government to ask what American reaction would be to that diversion program?

Ambassador **Yeutter**. I can't answer that question. I certainly did not discuss it with them, Senator Mitchell. Whether anybody at USDA did ahead of time, I really can't tell you.

Senator **Mitchell**. You had no knowledge of it? And on April 3, the Canadian Federal Government announced a major diversion program; and would your answer to that be the same?

Ambassador **Yeutter**. Yes. Yes.

Senator **Mitchell**. And on April 9, it was a joint federal and Province of New Brunswick diversion program of several million dollars, and you personally weren't contacted and you have no knowledge of anybody in this country being contacted?

Ambassador **Yeutter**. No. Of course, we don't talk to the Canadians about our diversion programs either.

Senator **Mitchell**. Well, I am leading up to that. We don't talk to them about our diversion program because we don't have one, and so there is nothing to talk about.

The problem is, you see, I think if you investigate thoroughly, you will find that of course the Canadians did not contact anybody in our Government to determine what our reaction would be to their acting on a diversion program. They did it because they felt it was in the best interests of their farmers, without any regard for any possible American reaction.

But when Senator Cohen and I asked our Government to provide a very modest diversion program, much smaller than what these Canadian diversion programs represent, the Secretary of Agriculture, a member of the administration, said to us: We can't do that. And one of the reasons cited was that we are concerned about the Canadian reaction if we adopt a diversion program.

And that is what really is troubling, Mr. Ambassador. It is that we won't act and help our farmers in part because we are worried about what the Canadians might think of it, while at precisely the same time the Canadians are acting, not once, not twice, not three times, but four times—three separate government entities—to act on their diversion program without the slightest bit of concern for us, nor should they have. I commend the Canadians. They are doing what they think is right for their people, and they are not so namby-pamby about it that they say, well, wait a minute, we had better go ask the Americans what are they going to think if we do this; they might not like this.

Meanwhile, we take the position that we will respond to our farmers not by dealing with their problems on the merit, but saying, well, wait a minute; what will the Canadians think if we adopt a program to help our farmers? To me, that really illustrates the whole problem with this approach. They do what they think is right and in their interest. They act aggressively without concern for our reaction; and again, I don't fault them for it. I say I commend them.

We, on the other hand, say, well, wait a minute; what will the Canadians think if we do that? And I must say that really troubles me. I know that is not your area, and you are not responsible for the diversion program; but I just want you to know what the roots of my frustration are.

Ambassador **Yeutter**. I can understand that, Senator Mitchell; but at the same time, I might draw a little, somewhat different conclusion than you did because I don't know whether or not the Canadian Government considered American reactions when they took those——

Senator **Mitchell**. I can guarantee you they didn't.

Ambassador **Yeutter**. Well, if they didn't, I would be critical of them because it seems to me that we are living in an interrelated world these days and that they should be concerned about reactions of their trading partners to programs such as that, and we ought to be concerned about reactions, too. We have to all live together in this world, and clearly we should do what is in our best interests; but we ought to be concerned about what impact that has on our trading partners, whether it be Canada or anybody else.

Senator MITCHELL. I would like to ask just a couple of specific questions. Canada has expressed the desire to be given special treatment under United States trade laws—antidumping, countervailing duties, 301, et cetera. What is your position on this?

Ambassador YEUTTER. My position on that, Senator Mitchell, is totally firm. That is an impossible request.

Senator MITCHELL. All right. Good. That is about the first good news we have heard this morning. Now, how do you plan to deal with the provincial problem that Senator Danforth identified and which is really a principal cause for concern? The diversion programs, I have mentioned. The major programs are provincial. It is not going to do any good if you reach an agreement with the Canadian Government; it has no effect on what the provinces do. And as you know, the provinces there play a much larger role in trade matters than do our States.

Ambassador YEUTTER. Yes. The Canadian Government, Senator Mitchell, is going to have to decide for itself how it wishes to handle that. Obviously, it can do it in a number of different ways. They can either have those provincial representatives at the negotiating table, or have some mechanism for their input with an assurance that they will buy off on whatever is agreed. This is a point that Senator Long was raising earlier. As I indicated earlier, they solved that problem in the Tokyo round and some of the other multilateral negotiations. So, I assume they can solve it here, too. How they plan to solve it this time, I don't know; but they know that we expect the provinces to agree to whatever is negotiated.

In other words, we are not going to negotiate individually with all of those provinces. We are going to negotiate with Simon Reeseman and his negotiating team, and we expect him to provide provincial signoffs on whatever it is we negotiate. If he doesn't have the provincial signoffs, obviously then we don't have an agreement.

Senator MITCHELL. My time is up. Mr. Chairman, I have several other questions that I would like to submit in writing because time doesn't permit them to be expressed orally. Will we be given that opportunity?

The CHAIRMAN. We will be given that opportunity although we will be voting on this midweek next week.

Senator MITCHELL. All right.

The CHAIRMAN. I also have a list of questions from Senator Wallop that he wanted submitted, and I will give them to you.

Senator DANFORTH. Senator Baucus.

[The prepared written questions of Senator Mitchell follow:]

[Responses not available at press time.]

Senator BAUCUS. Thank you, Mr Chairman. Mr. Ambassador, I have heard a lot of high-minded, well-meaning goals: free trade. You also spoke a bit about potential opportunities that American business and industry might have in Canada. That is very good, and I think those are opportunities that we should provide for our businesses.

The problem is that you have not addressed the reasons why Canada wants a free trade agreement; that is, what additional access they want to additional markets in the United States. You have not been specific about any of those areas. For example, let's take timber.

You know that 30 percent of the softwood today consumed in the United States is Canadian. Why? Basically, it is because Canada—the Provinces, particularly British Columbia from which most timber comes—subsidizes their stumpage. It is a very, very deep subsidy and a very direct subsidy. A good example of that is on the chart right over there.

It compares the stumpage prices of timber in various portions of the country, compared with the counterpart price just across the border in the corresponding Province. Now, those figures there are also weighted to include the same species of lumber, so there is no difference in the quality of the lumber reflected in the chart. You will see that the British Columbia stumpage price is $7 a thousand. In Idaho, just across the border, it is $53. Remember, it is the same timber. Those are weighted to take into consideration the same species and the same variety of timber.

Going further, right across that chart, in Washington and Oregon, what is stumpage? It is $108 a thousand. In British Columbia coastal, the rates are $20 a thousand; and the same applies across the rest of the chart. Again, that is the same kind of timber. That is the price differential due to the Canadian stumpage subsidy.

The next chart also shows what has happened to price compared with consumption. The dotted line on the top basically shows what American consumption of softwood timber has been. You can see that since 1982 consumption has taken a steep rise. I think that is basically due to the decline in American interest rates; housing is starting to take off again.

What has happened to the price in America? The price has fallen. At the very least, consumption is going up. You would think that with the law of supply and demand that the price at least would stay even in the same direction or maybe even go up higher; but no; it has fallen. Again, because of Canadian stumpage. And again, a big increase in stumpage prices that United States companies pay relative to the Canadians. In addition to that, not too many years ago, about 1976 or 1977, Canadian imports accounted for about 18 percent of American softwood consumption. Today, as I said, it is 30 percent. For 2-by-4's and for studs, it is in excess of 50 percent. At least 50 percent of the studs consumed and utilized in America today are Canadian imports.

Now, in addition to all that, we read reports in the Canadian press of how the Canadian timber industry has already spent $5 million to get a free trade agreement. They want something in addition to the status quo. In addition to that, you heard the statement referred to earlier of Prime Minister Mulroney in the House of Commons on March 21, who said: "We want more timber to go to the United States. More. More."

In addition to all that, we hear that one of our trade negotiators here in the District of Columbia—again reported in the Canadian press—said: "Don't worry about it; everything is fine. Congress is going to give a green light. Don't worry about anything."

I ask you: What specifically do you intend to accomplish in a free trade agreement that is going to stop this subsidy in Canadian stumpage? If I hear you correctly, you want a total free trade agreement. Well, then, doesn't that mean the total elimination of the Canadian subsidy on stumpage?

Ambassador **Yeutter**. OK. This is a very complicated issue, as you know even better than I, Senator Baucus, and one in which we have intense negotiations underway at the moment. My judgment is that this issue will be resolved long before we are very far underway with the free trade arrangement. So, it may not even be a portion of this, except in the sense that if we achieve the objectives that we have in mind with a free trade arrangement, timber trade will flow between the United States and Canada—timber products—on a free and open market basis; that is, with the trade being determined by economic fundamentals as it should be.

Senator **Baucus**. Does that include the elimination of the stumpage subsidy?

Ambassador **Yeutter**. Let me try to define the terms in a careful way so that I don't mislead anybody. What Canada is doing in its stumpage practices would be defined as a "subsidy" either under the present GATT subsidy code or under United States law; it is subject to some debate, as you well know. That term was considered by the Commerce Department in a case 2 or 3 years ago, as you know, and the definition in the GATT code is somewhat nebulous.

But suffice it to say, Senator Baucus, I will help you in this—suffice it to say that I consider it a legitimate trade problem that has to be solved and solved promptly. And it goes much beyond just United States-Canada, and it goes much beyond timber into other issues. We need to deal with the problem that is of concern to you, in the short run, promptly, bilaterally; and I am convinced that we will have that issue resolved to your satisfaction and to the satisfaction of the United States timber industry very soon, in terms of the United States-Canada bilateral relationship, unrelated to this comprehensive bilateral discussion.

We must then go beyond it and deal with the same issue in a multilateral context in a new GATT round.

Senator **Baucus**. I must say, Mr. Ambassador, I am not fully assured by that statement. It sounds very vague——

Ambassador **Yeutter**. Time will tell.

Senator **Baucus**. And that is one of the reasons why some of us are concerned. If I might, Mr. Chairman, I have just one other quick question here. Exchange rates. Are exchange rates on the table in any potential free trade agreement? As you well know, the United States dollar has fallen about 30 percent vis-a-vis the Japanese yen, and it has fallen significantly compared to other countries' currencies in the last couple of years. It has not fallen compared to the Canadian dollar. Canadians still enjoy a 30-percent discount. I suspect that is in part due to the softness of the Canadian economy, but I also suspect it is because Canada wants that 30-

percent discount to continue. They want to continue to flood the market.

It is a part of their trade policy. My question then: Are exchange rates fully on the table along with other trade matters in any potential free trade agreement?

Ambassador YEUTTER. That would depend, Senator Baucus, on whether we found that there was anything to negotiate with the Canadians about on that issue. And that really has to be Secretary Baker's lead on that particular point. I haven't discussed it with him. I discussed it with him in general, but I haven't discussed it with him with respect to this particular negotiation.

I don't want to preempt anything Secretary Baker might say on it. I have some personal familiarity with that issue from my days in the Chicago Mercantile Exchange where we traded Canadian dollars, as you well know, on a futures market; and my personal judgment, based upon that experience and my own background, is that there is no Canadian Government manipulation, if you will, of the exchange rate relationship; that that very weak Canadian dollar, troublesome as it is to us, is due primarily—almost entirely as a matter of fact—primarily is an understatement—almost entirely, if not entirely, to lack of an adequate level of economic performance in the Canadian economy.

And we can't negotiate that away. In other words, we can't negotiate a stronger performance by the Government of Canada.

Senator DANFORTH. Senator Grassley.

Senator BAUCUS. Thank you, Mr. Ambassador.

Senator GRASSLEY. Mr. Chairman, thank you. Mr. Yeutter, first of all, could I have the list of the 44 private sector advisory committees you referred to on page 2 of your testimony, their names, please?

Ambassador YEUTTER. Yes; certainly. There will be about 1,000 people.

Senator GRASSLEY. No, no. It says 44.

Ambassador YEUTTER. Yes; 44 committees with about 1,000 people in total.

Senator GRASSLEY. Well, can you give me that?

Ambassador YEUTTER. Certainly.

Senator GRASSLEY. I wasn't really asking for 1,000 names, but if that is what it is, you can give those to me. You must have them printed up some place.

Ambassador YEUTTER. Certainly.

Senator GRASSLEY. The first thing, I made my point in my opening remarks about this huge trade deficit, only second to Japan. And I want to know just a very short summary of why that is so huge; but that is not the main purpose of my first question. Is this free trade agreement—if one is arrived at and agreed to by both countries—is that going to make that tremendous trade deficit—Is it going to negate it? Leave it just about the same as what it is? Or is it going to be an even worse trade deficit for the United States?

Ambassador YEUTTER. Well, that is almost impossible to answer, Senator Grassley, because our assumption is that this negotiation or the results of this negotiation will be phased in over 10 to 12 years, which means that we really won't have that answer until the year 2000.

Senator Grassley. Well, then, what is your philosophy? Going into it without any care about whether or not there is a trade deficit between our countries?

Ambassador Yeutter. The trade deficit, Senator Grassley, is going to be dependent probably on the exchanges rates more than anything else. The principal reason that we have a huge trade deficit with Canada now is because we have a 70-cent Canadian dollar. If by the year 2000 we have it instead of at 70, it is at $1.30, I suspect we will have a trade surplus, but that depends on a lot of factors totally unrelated to this negotiation.

But if I didn't think this negotiation was in the best interest of your Iowa farmers, I wouldn't support it. I happen to think that we have substantial export potential resulting from this negotiation. Whether that will narrow the deficit or not, I am not sure. I certainly have no objection to Americans buying Canadian products if they would like to do so; and I am prepared to have us run a trade deficit with Canada if that be the will of the American people; but I certainly would like to open up additional export opportunities for American farmers and others. And I think we can do that.

Senator Grassley. All right. Let me ask you, then, to comment on three points that the farm bureau made; and the farm bureau in my State has the most membership. They feel that such agreements work against agricultural export interests. That is their first point.

And connected with that first point, they emphasize GATT; they feel that it is a violation of the most favored nation of GATT. The second point they make is they raise a concern that negotiation efforts will be made by the Canadian Government to exclude sensitive Canadian sectors and specific Government practices. As an example, an agreement that would allow the Canadian provinces free to regulate trade under their own authorities or an agreement that would allow certain Canadian domestic subsidy practices to continue to provide an unfair competitive edge to Canadian producers.

And then, lastly, the third one, they feel that an advantage of a truly effective free trade agreement between our two countries is that it should minimize the frequency of bilateral trade disputes. So, I need your comments on those points.

Ambassador Yeutter. I think there are very solid answers to all of those questions, Senator Grassley; and in fact, they are a very significant element of this negotiation.

With respect to pulling back on sensitive sectors, our hope would be that we keep everything on the table and that that not take place. Clearly, we are not going to let them pull back on sensitive sectors unless we also pull back on sensitive sectors; and we are trying to discourage that in both countries.

In terms of the effect of the provincial governments, we have already talked about that this morning. You know, we are going to expect the Canadian negotiators to bind those provincial governments; so we think that will take care of it.

In terms of whether it violates the most-favored-nation treatment, the ultimate product is going to have to not be violative of the most-favored-nation treatment. We will have an obligation under the GATT to make sure that doesn't happen. Conceptually, some people maybe are critical of this kind of bilateral because they feel that the United States and Canada will be, to some degree, taking advantage of the rest of the world; but we don't believe that is the case. In fact, we think it can set some examples for the rest of the world, and we believe we can negotiate it in such a way not to be a problem.

And in terms of what potential it has for your farm bureau constituents, Senator Grassley, that really depends on how we handle the agricultural negotiation, and that is what kind of changes in the Canadian system that we are able to negotiate and whether those will turn out to be a plus or a minus for Iowa producers. Having an agricultural background myself, I think you can tell them that I am not very likely to bring back an agreement that is going to look like it is a loser on agriculture. Otherwise, I am not going to go home to Nebraska.

Senator DANFORTH. Senator Chafee.

Senator CHAFEE. Mr. Chairman, thank you. I have to preside, but I would just like to say this: I am worried at the trend of the proceedings here today. I think, as the Ambassador indicated, this has ramifications of far greater dimensions than possibly most of us realize.

Second, I think that the Ambassador is being the recipient of a welling up of discontent not over our trade with Canada but our trade position generally and the feeling that the administration has not followed out on the desires and the admonitions that the Congress has expressed. We feel ignored, particularly in connection with Japan and the reciprocity clauses that we are seeking in connection with their activities, their nontariff trade barriers that they have erected against so many of our goods.

And I think it is unfortunate that Canada is somehow being the butt of all this. I think that this whole business deserves a thorough discussion, and we are going to hear further witnesses. I think that we don't want to set aside the potential of benefits to us. This isn't a one-way street; and they are a major trading partner with the United States. It is a country where our trade has increased.

And am I correct in saying that the imbalance hasn't always existed? The imbalance, I presume, has arisen with the great strength of the dollar. What was the trade situation, say, 5 years ago?

Ambassador YEUTTER. We have traditionally had a surplus with Canada. I can't tell you the numbers 5 years ago, Senator Chafee, but traditionally it has been in our favor and could well move in our favor again if the exchange rates begin to shift as could clearly happen.

Senator CHAFEE. And I would also like to say, Mr. Chairman, that somehow the idea that the Canadians want this, that therefore it must be bad for us, is not something I subscribe to. Thank goodness, we have got a commerce clause in the United States where there is trade between all our States, and we are all the beneficiaries of a larger market.

The United States can compete. We are not a helpless giant that can't sell our goods; and certainly, there are difficulties. But I think the problems that have been raised here should be considered in the negotiations; namely, provisions against subsidies and

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dumping. Now, do those provisions exist in the free trade agreement with Israel? There are provisions against subsidies and dumping, are there not?

Ambassador YEUTTER. Our existing antidumping laws continue to apply.

Senator CHAFEE. Sure. And so that isn't something that we are going to wave away. Now the problem of the provinces, I think, is very legitimate. You raised that. The provinces can raise a host of nontariff trade barriers to us, but somehow we can expect to look for those to be resolved; and if they are not resolved, then there is no deal. And I feel badly, Mr. Chairman, that positions seem to be hardened as I hear them expressed here today on a situation which I think holds great potential merit for the United States. There are problems; sure, there are problems, but that doesn't mean that the whole thing should be scuttled.

Ambassador YEUTTER. There is no question in my mind, Senator Chafee, that we are talking about the potential of billions of dollars of additional trade between the United States and Canada; a good bit of it moving from the United States to Canada. And I must say that the discussion this morning could well put all of that in jeopardy, which means that an awful lot of American businesses could be deprived of some very, very nice business opportunities.

Senator CHAFEE. Thank you. Thank you, Mr. Chairman.

Senator DANFORTH. I want to follow up, since I am next, on what Senator Chafee just talked about. Far from our position being hardened, I think the position of the members of the Senate Finance Committee for the past 5 years has been that we are open for business with the administration, that we want to talk with the administration. We want to deal with the administration, and we want to work out problems with the administration.

I think that the position of the administration toward us has been: get lost. And I think that in a very diplomatic way, Mr. Ambassador, in a very diplomatic way, that is the substance of your comments to us today. What you have said to us today is that even at this hearing by raising questions about whether we want to go forward with this negotiation, that it has—as you have said—major implications for United States-Canada relations. Those were your words.

Ambassador YEUTTER. Yes.

Senator DANFORTH. You said there would be 6-inch headlines about what we say today. Now, it would follow, I would think, that if what we say today is something that will produce 6-inch headlines, then there would be 12-inch headlines if the administration were to spend 2 years in negotiations with Canada, and then after you came back to us, we turned you down. So, if we can't assert our position today because it has implications on United States-Canada relations, it follows that we shouldn't be asserting ourselves after the negotiations are completed.

I think what you are saying to us and what the administration has been saying to us right along with respect to any legislative ideas that are held by members of this committee or Members of the Congress—what I really believe what your message says—is: Keep your cottonpicking hands off trade.

Ambassador **Yeutter**. I don't think that is a fair assessment, Mr. Chairman. I really don't. That certainly doesn't reflect my attitude, and you know that.

Senator **Danforth**. I am not saying you; I am saying the administration. The prevailing sentiment in the administration is to stonewall trade, not to deal with the Congress. It is basically the same position the administration has on the budget: not to deal with Congress, not to be flexible, not to come to the bargaining table with us, not to work out the difficulties that we see in international trade.

Ambassador **Yeutter**. Well, putting aside the legislative scene for a moment, because that, obviously, has different dimensions from the issue that is present here, I would simply say that I am not at all fearful about a potential turndown from this committee, once we bring back a negotiating result. I have enough self-confidence to believe that the package that we bring back to you, Senator Danforth, will be one that you would endorse with enthusiasm because I am not going to bring it back unless I feel that you will endorse it with enthusiasm. So, I am prepared to take that risk 2 years down the road or whatever it is.

But to say now that you will not grant fast-track authority, it seems to me, colors the entire negotiating environment in a way that could frustrate the results.

Senator **Danforth**. When do we weigh in if it is not now? What leverage do we have if we don't use it now?

Ambassador **Yeutter**. You certainly have an opportunity to use leverage all through the process in the way that Senator Long was talking about earlier, in the manner in which you worked with Bob Strauss during the final stages of the Tokyo round. Even though you were on a fast-track procedure there, I am sure that you and others had a lot of discussion with Ambassador Strauss; and I am sure he paid due attention to what you had to say before that package went into final form.

Senator **Danforth**. That was a different administration.

Ambassador **Yeutter**. Well, I think my modus operandi is very similar to the modus operandi of Ambassador Strauss.

Senator **Danforth**. I am not questioning you. I am saying that this is the position of the administration. The administration's position is that they have made up their minds; their ideology is locked in concrete. They are saying: Don't bother us with any views that you have.

Ambassador **Yeutter**. I really don't believe the administration is that inflexible, Senator Danforth. You know, clearly the administration has some differences of viewpoint on budget reconciliation and trade issues and other things; but I don't believe we are quite as rigid and inflexible as those comments may have indicated.

Senator **Danforth**. All right.

Senator **Pryor**. Mr. Chairman, if we have to go and vote—and they are adhering to the strict 15-minute rule—are you going to let the Ambassador leave before we get back?

Senator **Danforth**. No; I hope not.

Senator **Pryor**. You are going to lasso him and keep him here a little longer?

Senator **Danforth**. Yes.

Senator **Pryor**. Thank you. Thank you. [Laughter.]

Ambassador **Yeutter**. OK, Dave.

[Whereupon, at 11:41 a.m., the hearing was recessed.]

AFTER RECESS

The **Chairman**. The committee will come back to order, please. Mr. Ambassador, I will tell you what I would like to do. As I left, several members said: Don't let him leave; don't let him leave. And I think there is going to be another vote right after this one.

If you wouldn't mind just stepping aside a moment and letting me take another panel and see if I can get through them before I have to go to vote; and by that time, the fellows will be back and will be ready to ask you questions.

The lumber panel said they just want to submit their statements for the record?

Mr. **Dennison**. Mr. Chairman, we would like to make some brief remarks, but not our full remarks.

The **Chairman**. Come right up.

We have Mr. Stanley Dennison, chairman of the Coalition for Fair Lumber Imports; Mr. J.M. Tolleson, Jr., president of Tolleson Lumber Co. of Perry, GA; and Mr. M.J. "Gus" Kuehne, executive vice president, Northwest Independent Forest Manufacturers. You have been very patient, fellows. I appreciate it.

STATEMENT OF STANLEY S. DENNISON, CHAIRMAN, COALITION FOR FAIR LUMBER IMPORTS, ATLANTA, GA

Mr. **Dennison**. Good morning, Senator. Thank you for this opportunity to testify on the negotiations for United States/Canada free trade agreement. We will make our comments very brief. We think they have been very well stated by you and by the other Senators this morning.

We feel that if we wait another 2 years for relief from Canadian timber subsidies, we will lose another 5 to 10 percent of our lumber business. Our mills, our jobs, and our forests will further decline. The Canadians, through their subsidies, are liquidating our industry, year by year. We have consistently urged a refusal of fast-track approval unless significant progress was made toward relief from the flood of Canadian timber entering our country.

Senator, I thank you.

[The prepared written statement of Mr. Dennison follows:]

STATEMENT OF

STANLEY S. DENNISON
CHAIRMAN
COALITION FOR FAIR LUMBER IMPORTS
WASHINGTON, D.C.

COMMENTS ON PROPOSED
U.S. - CANADA FREE TRADE AGREEMENT

BEFORE THE

UNITED STATES SENATE

FINANCE COMMITTEE

APRIL 11, 1986

GENERAL

Good morning. My name is Stanley S. Dennison. I am Chairman of the Coalition for Fair Lumber Imports. The Coalition is comprised of major U.S. softwood lumber manufacturers associations and represents more than 70 percent of U.S. lumber production. I appreciate this opportunity to comment on the proposed U.S. - Canadian Free Trade Area.

As you are aware, the lumber industry is very important to the U.S. economy. Almost 8 million individuals own over 346 million acres of timber land. In 1984, 704,130 individuals earned a total of $11.9 billion in the lumber and wood products industry. Another 676,207 individuals, earning $17.5 billion, are employed by the paper and allied products industry, which is interrelated to the solid wood products industry. Clearly, the health of the forest products industry impacts our national economy. Attached for the record are two tables displaying ownership, employment, and earnings in the United States.

The U.S. lumber industry by any measure should be enjoying good times. The consumption of softwood lumber is at record levels, fueled by a strong housing market and by record usage of softwood lumber in uses such as home repair and remodeling. Yet despite this record consumption, the U.S. lumber industry faces disaster. The U.S. lost a net 629 softwood lumber mills between 1977 and 1984, and mill employment dropped by 30,000. In 1984, the industry had pre-tax losses of over $300 million and wrote off over $600 million in assets.

The primary reason for the problems faced by the U.S. lumber industry is the flood of subsidized Canadian lumber into the United States.

Canadian producers and government representatives put forth a number of arguments to explain their progressively increasing share of the U.S. lumber market. These arguments will be discussed by my colleagues. However, none of those arguments explain the real problem faced by the industry. Why, in record demand years, is the domestic industry in such poor economic condition?

The Canadian government has initiated the request for negotiations for a free trade agreement between the United States and Canada. For the domestic lumber industry, however, it is important that negotiations for a free trade agreement be preceeded by significant progress towards a resolution of a devastating problem -- that of undervalued Canadian lumber imports.

The Coalition is not alone in its recognition of the problem caused by Canadian lumber imports. Last October, ten members of the Senate Finance Committee urged U.S. Trade Representative Clayton Yeutter to "seek an early resolution of the softwood lumber trade issue" in order to facilitate consideration of a free trade agreement with Canada. They said that "any free trading agreement must be built on a foundation of fair trading practices."

A month later, 63 members of the U.S. House of Representatives urged Secretary of State George Schultz to "elevate the issue of unfair Canadian timber subsidies to a position of central prominence prior to entering into negotiations for a free trade agreement with Canada." They said further that "efforts to reach a bilateral trade agreement between our two nations should not proceed until both sides address the Canadian lumber subsidy issue."

In response to these pleas and others, on November 26, 1985, Ambassador Clayton Yeutter initiated high level talks with Canada on the lumber dispute. United States negotiators are working to solve the major problem of the domestic lumber industry, the noncompetitive stumpage pricing policies of the Canadian provincial governments.

To date, however, there is no indication that the Canadians are willing to eliminate the benefit they receive from their timber subsidies. For this reason we believe the Senate Committee on Finance should withhold negotiating authority for the free trade agreement in light of Canada's unwillingness to make significant progress toward resolving the lumber issue.

The Canadians believe that the lumber issue should be folded into the overall negotiations for a free trade agreement. This is simply a stalling tactic on the part of Canada. The U.S. lumber industry, and the communities and families that depend on it, simply can not wait the length of time needed for the extensive negotiations of the free trade agreement. We are not against free trade. However, our need for fair trade is immediate. The domestic lumber industry faces a crisis. It is therefore vitally important that negotiations for a free trade agreement be preceeded by significant progress towards a resolution of the Canadian lumber import dispute, and imperative that the lumber problem not get folded in to protracted trade negotiations.

1984 EMPLOYMENT AND WAGE STATISTICS BY REGION
LUMBER AND WOOD PRODUCTS, AND PAPER AND ALLIED PRODUCTS

	TOTAL	South	West	Northeast	Midwest
EMPLOYMENT					
Lumber & Wood Products	704,135	311,852	209,658	80,494	102,131
Paper & Allied Products	676,207	217,716	72,769	197,808	187,914
Subtotal	1,380,342	529,568	282,427	278,302	290,045
TOTAL WAGES ($000)					
Lumber & Wood Products	11,945,536	4,481,117	4,480,256	1,271,671	1,712,492
Paper & Allied Products	17,473,302	5,576,149	2,034,968	4,819,930	5,042,255
Subtotal	29,418,838	10,057,266	6,515,224	6,091,601	6,754,747

Source: U.S. Bureau of Labor Statistics

U.S. PRIVATE TIMBER OWNERSHIPS AND ACREAGE BY REGION

Region	Number of Private Owners	Acreage
South	4,033,300	194,886,100
West	714,270	46,107,100
Northeast	1,646,600	59,959,400
Midwest	1,357,400	45,376,400
TOTAL	7,751,570	346,329,000

Source: USDA Forest Service, Northeast Station
(From unpublished data)
Note: Forest Service totals adjusted for reports by state foresters.

STATEMENT OF J.M. TOLLESON, JR., PRESIDENT, TOLLESON LUMBER CO., PERRY, GA

Mr. TOLLESON. Thank you, Senator. I am J.M. "Buddy" Tolleson from Tolleson Lumber Co. in Perry, GA. I might, for your benefit, say that, in Perry, we have eight plants. We are headquartered in Perry, a town of about 10,000 people. It is the hometown of your colleague and our mutual friend, Sam Nunn.

The CHAIRMAN. You have eight plants in a town of 10,000?

Mr. TOLLESON. No; in three Southeastern States, but we are headquartered in Perry, a town of 10,000, which happens to be the hometown of Senator Nunn. I thought it might be interesting also for you to know that this old Georgia sawmiller has served for 14 years as the chairman of the Sam Nunn Senate Campaign Committee. [Laughter.]

So, I have got tougher things than sawmilling. [Laughter.]

Senator, I just want you to know, and I would like the whole committee to know, that I have been observing your talks this morning and your support and that we feel warm and solid about the feelings of this committee and the big task it has confronted it protecting people like us all over the South who have a terrible situation in this inundation of Canadian lumber. We are very appreciative of your support. We feel in listening to Ambassador Yeutter today that maybe the whole store would be given away.

Your support and the support of this committee has warmed us and made us feel solid today. I appreciate it very much.

The CHAIRMAN. Thank you, sir. Mr. Kuehne.

[The prepared written statement of Mr. Tolleson follows:]

STATEMENT OF

J. M. TOLLESON
PRESIDENT, TOLLESON LUMBER COMPANY
PERRY, GEORGIA

COMMENTS ON PROPOSED U.S. - CANADA FREE TRADE AGREEMENT

BEFORE THE

UNITED STATES SENATE

FINANCE COMMITTEE

APRIL 11, 1986

Good morning, I am J.M. "Buddy" Tolleson. I am President of Tolleson Lumber Company in Perry, Georgia. I appreciate this opportunity to testify regarding the serious problem of undervalued Canadian lumber imports.

The problem of unfair lumber imports from Canada is of growing concern to the U.S. South where forestry and related economic activities provide $10 billion in wages to over 500,000 employees.

Alabama, Georgia and North Carolina are among the largest timber producing states in the nation. However, more than 50 percent of all lumber sold in those states is Canadian.

Furthermore, unlike the timberland in the Northwest, which is largely owned and administered by the National Forest Service, fully 75 percent of our timberland is privately owned. That means that the fruits of a prosperous timber industry, or the pain of one on the losing end of unfairly subsidized competition, is distributed widely and deeply throughout the South.

The bulk of the timber consumed in the United States is grown on private lands. After mature timber is cut, the land is prepared and replanted with nursery-grown seedlings. The stand is managed over the next 30 to 60 years before the harvest of the next "crop" of mature timber. The price of timber in the U.S. therefore is not arbitrary; it reflects a recovery of, and modest profit on, this extended investment.

In contrast, almost 95 percent of Canadian timberlands are owned by the provinces. Timber is sold at arbitrarily low prices to ensure employment. In some provinces, the government assumes most of the cost of forest regeneration. In our opinion, this practice of selling timber at a price which does not recover the cost of such basic management responsibilities, and far below the price that Canadian timber would sell for in the market, constitutes a subsidy. In other provinces, little is done to regenerate the forest, by the companies or the government. Current Canadian fees for timber cutting rights simply cannot cover the cost of significant reforestation. This seems shortsighted from a resource conservation viewpoint.

Over the last 35 years, private U.S. landowners have converted over 35 million acres of woodland from natural growth to high-productivity, high quality stands. Known as "intensive forestry management," this practice has helped make the United States the woodbasket of the world, with fiber growth equalling or exceeding fiber consumption for both paper and wood products.

Under current conditions of depressed lumber prices caused by a flood of undervalued Canadian lumber, the only avenue of survival for U.S. lumber producers is to pay less for timber. In time, we foresee U.S. timber prices dropping to a level at which intensive forestry management will have to be abandoned, with the woodlands reverting to lower-quality, lower-yielding natural stands. Harvesting of timber on U.S. lands will fall as U.S. mills will be unable to pay a fair value for timber and continue to compete agianst subsidized Canadian mills. Longer term, this could reduce both the volume and quality of wood fiber grown in the U.S., with a potentially significant impact on the $10 billion wood products and paper industries, including possible loss of an additional 15,000 forestry jobs.

The U.S. lumber market is booming, but the U.S. lumber industry, one of the most efficient in the world, faces economic disaster. Tens of thousands of lumber workers are out of work. Hundreds of mills are closed. The cause of these problems is depressed lumber prices caused by severe overproduction.

Canada is the source of overproduction. Canadian production increased by 103 percent since 1975 while U.S. production increased only 20 percent. Over two thirds of Canadian production is shipped to the United States. As a result, Canada's share of the U.S. market rose from 18.7 percent in 1975 to 33.5 percent in the first nine months of 1985.

Canadian provincial governments induce production to promote employment. Since the provinces own more than 90 percent of

Canadian timber, they can give it to producers at prices well below fair market value. When Canada exports its lumber to the United States it, in effect, exports its unemployment.

Canada's overproduction is induced by unnaturally low prices for stumpage. Since Canadian lumber firms pay a noncompetitive price for raw materials, Canadian production is not disciplined by market forces. Canadian firms receive stumpage for a small fraction of what U.S. firms pay for comparable stumpage. There is no reason for similar trees on similar terrain immediately north and south of the border to be priced so much lower in Canada.

The Canadian system induces inefficiency because it is noncompetitive. High average logging costs translate directly into even lower stumpage.

Canadian stumpage payments are so low that they do not even cover the cost of basic silviculture. Correspondingly, Canada's forests are being liquidated; its production is expected to fall dramatically in 10-15 years.

By then, however, the U.S. industry will be in ruin. The net effect is that Canada's short-term employment policies are ruining the U.S. industry and, in the long term, denying the American consumer a stable, reasonably-priced supply of lumber.

STATEMENT OF M.J. "GUS" KUEHNE, EXECUTIVE VICE PRESIDENT, NORTHWEST INDEPENDENT FOREST MANUFACTURERS, TACOMA, WA

Mr. KUEHNE. Mr. Chairman, I want to thank you at the outset for the efforts that were made by you and the other members of this committee in the fall of 1981 to first explore the problems with imported Canadian lumber. Since that time, there has been a great deal of study, a great deal of talk, and a great deal of lumber flowing over the border.

This should be a time of unprecedented prosperity in this industry because it is a time of unprecedented demand for lumber products in this cyclic industry. We have never had a higher level of consumption of lumber in the United States than was achieved last year. The year 1984 was also a record year for lumber consumption, yet 1985 consumption exceeded it by 900 million board feet. That is the good news.

The bad news is that the Canadian imports not only took up all of the increase, but they set back companies and mills in the Western United States, where production diminished by 400 million board feet. An ITC study just recently released showed that mills in the State of Washington, which I come from, were the most productive mills in the United States or Canada.

Instead of a gain of some 27,000 jobs, which would have occurred given the increase in lumber consumption in the United States in 1984 and 1985, we have suffered a loss of 15,000 jobs; one-third of those being in logging and manufacturing, with the others in indirect jobs.

We appreciate the position that members of this committee have taken here today and hope that this issue will be resolved and give the administration the strength that it needs to negotiate a solution to this problem.

Thank you.

[The prepared written statement of Mr. Kuehne follows:]

STATEMENT OF

M. J. KUEHNE
EXECUTIVE VICE PRESIDENT,
NORTHWEST INDEPENDENT FOREST MANUFACTURERS
TACOMA, WASHINGTON

COMMENTS ON PROPOSED
U.S. - CANADA FREE TRADE AGREEMENT

BEFORE THE

UNITED STATES SENATE

FINANCE COMMITTEE

APRIL 11, 1986

Good morning. I am M.J. "Gus" Kuehne, Executive Vice President of the Northwest Independent Forest Manufacturers, based in Tacoma, Washington. I appreciate this opportunity to testify before this Committee, regarding trade in lumber between the United States and Canada. I would like to thank the members of the Committee, and especially the distinguished Chairman, for the interest that you have shown in this matter of deep concern to the nation's lumber industry. The economic vitality of the northwest is inextricably linked to the health of that industry.

The growth in Canadian softwood lumber production has been directly linked to growth in Canada's share of the U.S. market. In 1975, with production of about 11 billion board feet, Canada enjoyed about 19 percent of the U.S. market. In 1985, with about 21 billion board feet of production, Canada controlled about 34 percent of our market.

Canadian industry and government officials argue that their lumber can be sold at prices considerably lower than U.S. lumbermen can meet because of better mill productivity, and because of transportation cost advantages.

However, a 1985 report of the U.S. International Trade Commission concluded that U.S. and Canadian mills making similar products are nearly equal in productivity. And it is the U.S. producers who enjoy a transportation advantage because production facilities are closer to major markets. In Canada, plants are more remote, further from their customers.

Canada claims that a species preference for Spruce-Pine-Fir over Southern Yellow Pine lumber has caused the dramatic increase in its share of the U.S. market. However, that argument ignores the fact that the western spruce-pine-fir sold by Canada is also produced and sold in the western and northeastern United States. Yet, the flood of Canadian shipments has most severely displaced those U.S. producers of that comparable western lumber. In addition, if there is a species preference for Canadian lumber, all things else being equal, Canadian timber should be more valuable, and more expensive, than that in the United States.

There is a simple reason why Canadian lumber producers have been able to increase production during the most depressed lumber market in U.S. history and take a large portion of U.S. manufacturers' market share. The same reason allows Canadian lumber employment to remain high in this no-profit market while U.S. competitors are facing ruin: Canadian lumber producers pay little or nothing for their timber raw material.

All but seven percent of Canadian softwood timber is owned and sold by provincial governments. Government policy sets the price of standing timber, usually referred to as stumpage, at extremely low costs to help local lumber producers maintain employment. A 1982 study by the U.S. International Trade Commission recognized that the artificially low cost of Canadian stumpage is the primary cause of the lumber trade imbalance.

A 1985 ITC report stated that on average, provincial timber is provided to Canadian mills at $92 per thousand board feet less than U.S. stumpage, adjusted for the current exchange rate. But, as large as that differential is, it doesn't tell the whole story because it compares timber of different characteristics and growing conditions. For an accurate picture of the situation, it is important to look at areas where roughly comparable growing and tree harvesting conditions exist.

Lumber mills in Idaho harvest from exactly the same forest as Canadian manufacturers just across the border. Canadian mills pay an average of $46 less per thousand board feet -- a difference of about 85 percent in that region. Cross-border comparisons between Washignton and Oregon states and British Columbia on the coast show a $87 advantage to the Canadian buyer, a difference of 80 percent in timber costs. In Ontario, comparable figures are $9 and 33 percent; in Quebec, they are $32 and 73 percent.

Canadian officials have attempted to justify lower timber prices partly on the grounds that U.S. logging roads are better and harvesting conditions are less costly below the border. But these differences, if any, have been eliminated in the specific cross-border comparisons.

The difference in Canadian government timber prices and fair market value that emerges from cross-border comparisons is further demonstrated in Canada by similar differentials between Canadian stumpage on the one hand and private timber sales and competitive government sales on the other. Moreover, two other factors emphasize the absence of fair market value in Canadian stumpage: (1) the cost of growing the timber, including forest regeneration, is not recovered by Canadian stumpage fees; and (2) the lack of price fluctuations and continuing increase in production in Canada regardless of the demand for lumber.

Stumpage subsidies, however, are only one element in a pattern of unfair government interference in what should be a free market. A recent press announcement reporting on the plans of an American company to build a new waferboard plant in British Columbia instead of Oregon provides evidence. Some of the reported reasons for investing in Canada include $25 million in low-interest loans from the B.C. government, and a 20-year license to harvest timber. The production of that mill will be sold primarily in the U.S. market. Competing U.S. mills are not provided with comparable governmental assistance.

In conclusion, Mr. Chairman, lumber is traded between the United States and Canada under existing market conditions which can be viewed as free trade, but surely not as fair trade.

The CHAIRMAN. I think, deep down, there is a fair number that would secretly say: You bet. Give us this club in our hands, and we can go back to the Canadians.

And it isn't just the Canadians; go back to the Japanese. Because what happens if we vote this resolution down next week is that that is going to be felt in Tokyo also, in addition to Canada. So, I am very hopeful that we will go ahead with the resolution of disapproval.

You put your finger on it—all three of you—on a very interesting point. There is no reason, if we get 2 million housing starts this year and we may get 2 million housing starts, and if we get our budget and interest rates drop another half of a percent or a percent, and we get two or three million housing starts, there is no reason given that why this shouldn't be the best year in the history of American lumber. And it could be even in a free trade situation.

I don't hestitate to have my mills in the Northwest go toe to toe with the Canadian mills; and my hunch is that the mills in the Southeast would do very well head to head with the Canadian mills on a straight free trade, no subsidy there, no subsidy here basis. We don't have that.

And I don't sense we are going to get that out of any negotiations if we start down a fast-track road. So, I just think we would be very wise to say to the administration, without any malice—we are not being mean to the Ambassador or trying to stick our finger in the President's eye—just say: Go back and negotiate with the Canadians for 3 or 4 or 5 months. Come back to us and tell us what you have got before you make this request to start down the road on a fast track.

And if in 4 or 5 months or 6 months or 7 months—you know, that is not a long time in the history of this Republic—if the signs are more hopeful, things may change. But I do not see how we can go ahead under the present circumstances.

Gentlemen, thank you very much. You have been very patient.

Mr. KEUHNE. Thank you, Senator.

The CHAIRMAN. Let's go to the other panel and see what happens. You have set a very good example. [Laughter.]

Let's go with Mr. Nichols, Mr. Fox, Mr. McMinn, and Lucy Sloan. Miss Sloan has been before this committee on occasion and any number of other hearings I have conducted involving fishing matters. Good to see you again, Lucy.

Ms. SLOAN. Thank you, Senator.

The CHAIRMAN. Go right ahead, Mr. Nichols.

STATEMENT OF CARLTON E. NICHOLS, PRESIDENT, AMERICAN FURNITURE MANUFACTURERS ASSOCIATION; AND PRESIDENT, NICHOLS & STONE CO., GARDNER, MA

Mr. NICHOLS. Thank you, Mr. Chairman. Members of the committee, my name is Carlton E. Nichols, Jr., and I am president of Nichols & Stone Co. of Gardner, MA, and I am serving this year as president of the American Furniture Manufacturers Association. I am pleased to submit these views on behalf of our association on an issue of very vital concern to our industry; that is United States-Canada trade, the free trade agreement.

I understand that my full statement will be made a part of the hearing record, and I will summarize it in my testimony. Let me, if you will, digress for a moment very briefly from United States-Canada trade to paint you a picture of the domestic furniture industry. The 1980's, once predicted to be the golden age of furniture manufacturing, based on baby boom demographics, have instead featured declining furniture employment and a 470-percent increase in U.S. furniture imports to the level of $2.6 billion.

In short, our industry is under a great deal of import stress. Our response to significant import presence in the U.S. market has not been to call for import quotas or take a protectionist stance. The furniture industry is and always has been extraordinarily competitive and the underpinning of our trade policies has been to allow the U.S. industry to compete fairly on even terms with those countries internationally competitive in furniture products. To that end, we strongly support the negotiation of a free trade agreement between the United States and Canada, and more specifically, free trade on furniture products.

To date, the administration has been most responsive to our Canadian tariff problem. It is my understanding that the administration fully intends to seek a resolution of this matter during the United States-Canadian free trade negotiations, should they occur. My complete statement provides further information on why the existence of Canadian furniture tariffs fully five. times that of the United States level is unjustified, and a 1984 United States ITC study of our industry indicates the same.

Suffice it to say that the skewed marketplace resulting from the tariff inequity cannot be allowed to continue unabated. The 1985 increase in wood furniture imports from Canada was 54 percent. Overall, in 1985, our furniture trade deficit increased $100 million to a level of $350 million.

Canadian furniture represents 16 percent of all United States furniture imports. While these numbers may not seem inordinately large to a committee accustomed to dealing with billions of dollars, please keep in mind that there are only a handful of firms in the entire furniture industry grossing more than $350 million annually. And over two-thirds of the firms in our industry employ 20 people or less. AFMA strongly supports the Fair Furniture Trade Act, S. 1801, H.R. 3644, as providing a strong and credible incentive toward free trade on furniture products between the United States and Canada.

If free trade negotiations prove unsuccessful, United States furniture tariffs would be gradually increased until they were even with the Canadian level. And as our statement points out, at no time would United States tariffs ever exceed the Canadian duties level. Also, if Canadian tariffs were reduced, then United States tariffs would be reduced accordingly.

In summation, AFMA urges the committee to allow the administration to proceed toward negotiations to what we feel could be truly a historic agreement. I thank you.

The CHAIRMAN. Thank you, sir. Mr. Fox.

[The prepared written statement of Mr. Nichols follows:]

STATEMENT OF CARLTON E. NICHOLS, JR.

PRESIDENT

AMERICAN FURNITURE MANUFACTURERS ASSOCIATION

ON

U. S. - CANADA FREE TRADE NEGOTIATIONS

SUBMITTED TO THE

SENATE FINANCE COMMITTEE

APRIL 11, 1986

Mr. Chairman, Members of the Committee, my name is Carlton E. Nichols, Jr., and I am President of Nichols and Stone Company of Gardner, Massachusetts, and am serving this year as President of the American Furniture Manufacturers Association (AFMA). I am pleased to submit these views on behalf of AFMA with regard to an issue of critical importance to our industry -- the negotiation of a U.S./Canada free trade agreement.

The American Furniture Manufacturers Association is the largest furniture manufacturing trade association in the United States. By volume, sales by AFMA member companies comprise the vast majority of residential furniture produced in the United States. Also, the AFMA members have home offices or facilities in almost the entire fifty states and provide employment to several hundred thousand persons.

I would like to state the association's strong support for a free-trade agreement on furniture products shipped between the United States and Canada and support for the Fair Furniture Trade Act, S. 1801 and H.R. 3644. For years AFMA members have urged the Congress and the Administration to do everything possible to have furniture tariffs between the United States and Canada put on a more equitable basis.

After all the time and effort our industry has devoted to resolving this continuing issue, we would hope that the U.S. and Canada will act quickly to effectuate a trade liberalization agreement providing free trade, or equal duties, at a minimum, for furniture products between our two countries. If not, as discussed below, the mechanism included in the Fair Furniture Trade Act will work to provide reciprocal tariff treatment on Canadian furniture entering the U.S.

The Administration's desire to enter into bilateral trade negotiations with Canada currently hinges on whether the negotiations are blocked by the Senate Finance and House Ways and Means Committees. I urge you and the Committee not to disapprove this proposal.

AFMA believes that our two countries stand poised to enter into a potentially historic agreement. While we recognize that ours and other industries have long-standing grievances regarding trade with Canada, AFMA sees the proposed negotiations as a landmark opportunity for both countries to resolve disputes. It is our fervent hope that a "one-issue" focus will not jeopardize these negotiations.

A number of statements have been made by Canadian officials which indicate that the Canadian Government intends to push for a long-term, gradual reduction in

Canadian tariffs during the proposed bilateral negotiations.

The U.S.-Canada furniture trade deficit today stands higher than it has at any other time in the history of U.S.-Canadian trade (approximately $350 million in 1985), with a rate of increase in wood furniture of 54% in 1985. Given the added effect of the persistently overvalued U.S. dollar, which has yet to decline relative to the Canadian dollar, AFMA believes that the American furniture industry cannot afford a prolonged phase-in period. With regard to trade policy, we believe that Canada, which has the highest tariff walls of any major industrialized nation, should stop "acting" as if it were an advanced country and promptly start "being" one.

AFMA is extremely concerned with tariff barriers which have been set by a number of countries with the intent of keeping furniture manufactured in the U.S. out of their domestic markets. The United States, on the other hand, has maintained low tariffs on furniture. In fact, the record of the U.S. on domestic tariffs has been outstanding: duties on wood and upholstered household furniture entering the U.S. have decreased by 73% and 76% respectively, since 1963, and by 1987 will have decreased 76% and 80%, respectively (under the Multilateral Trade Negotiations). The record of certain other countries in that regard has not been as commendable.

Because of our common border, similar cultures and government regulations, Canada provides the American furniture manufacturer with perhaps the most egregious example of unfair tariff barriers to U.S. products in the world. Non-metal, residential furniture shipped from the United States into Canada faces a minimum duty of 15.6%. Canadian furniture entering the United States faces duties of 8.3% (upholstered), 5.7% (wood chairs), or as low as 2.8% for the bulk of furniture products (wood tables, desks, beds, etc.). Therefore, through duties assessed, Canadian furniture imports are given a clear and substantial advantage over U.S. exports to Canada.

The effect of inequitable Canadian duties, coupled with an unfavorable exchange rate, on the U.S. furniture industry has been dramatic. According to the U.S. Department of Commerce, U.S. imports of Canadian furniture rose from $149 million in 1980, to $428 million in 1985 -- almost a 187% increase. The $428 million 1985 figure - 16% of all U.S. furniture imports -- represents a growth of 25% from the 1984 total of $344 million. But U.S. furniture exports to Canada continued to decline in 1985 ($78 million) -- down by $15.4 million from 1980.

For 1985, U.S. Department of Commerce import/export data on the Canadian/U.S. wood furniture trade is highly disturbing. Canadian wood furniture shipments into America grew $40 million from 1984-85, from $150.2 million to $190.9 million. At the same time, U.S. wood furniture exports to Canada dropped by approximately $13 million, from $46 million to $33.6 million. As previously mentioned, these 1985 figures demonstrate an astounding 54% increase in the Canadian/U.S. wood furniture trade deficit when compared with 1984.

Going beyond Canada, for a moment, and using the most recent U.S. Department of Commerce data available, wood and upholstered furniture imports from 1979 to 1985 increased 470.6% from $312 million to $1.78 billion. U.S. exports of the same categories from 1979 to 1985 went from $312 million to an estimated $170 million. Taken together, these trends are forecasting a fundamental restructuring of the U.S. furniture industry, based not on a valid competitive balance, but upon an international marketplace skewed by tariff barriers.

Plant closings and employment figures also illustrate the impact these barriers can have, beyond the U. S.-Canada furniture trade deficit. While the full blame for adverse employment effects and plant closings cannot be laid solely to Canadian imports, they obviously have played a significant role, as Canada is America's second largest furniture importing country. According to the most recent U.S. Department of Commerce statistics, the U.S. wood furniture industry lost 375 manufacturing facilities over the 1977-1982 period, while the U.S. upholstered furniture industry lost 246 manufacturing facilities over the same period -- a total loss of 621 facilities. As a direct consequence, according to the U. S. Department of Labor's data, U.S. wood furniture manufacturing employment declined from 147,000 in 1979 to 132,400 in 1985, and upholstered furniture manufacturing employment dropped from 101,700 in 1979 to 94,500 in 1985.

These numbers reflect the extent to which the Canadian-U.S. tariff inequity forces competition to be on a most unfair and uneven basis. Competition is an essential element of our business. This industry is not, nor has it ever been, dominated by a few large companies. Instead, it is an extraordinarily competitive industry comprised of approximately 4500 companies, over two-thirds of which employ fewer than 20 workers. Profit margins are slim (since 1978, after-tax profits have averaged approximately 3-4%). Estimates are that the wood and upholstered furniture industry had approximately $11.2 billion in shipments during 1985.

In 1984, the International Trade Commission (ITC) completed a study, entitled, Competitive Assessment of the U.S. Wood and Upholstered Household Furniture Industry. The study was comprehensive and well-documented, and the published report provides an overview of the industry's current domestic and international trade position. We were pleased to have many of our members contribute to that study and to have the Commission in High Point, N. C. for field hearings and tours of furniture facilities.

The ITC report pointed out that, historically, the U.S. and Canada have been major furniture trading partners. In fact, while Canada is among the leading exporters of furniture into the U.S., it is also the second largest importer of U.S. furniture.

The Canadian furniture industry is very similar to the U.S. industry in structure, wages, level of technology and access to capital. Much like the U.S., worker health and safety and pollution control are deemed essential in Canada, and thus regulated by government. The ITC study of our industry documented the similarities between the U.S. and Canadian industries in the description of "Major Foreign Competitors," (Competitive Assessment of the Wood and Upholstered Household Furniture Industry, U.S. International Trade Commission, Publication 1543, pp. 21-22).

U.S. furniture manufacturers have enjoyed no special protection. Canadian manufacturers, on the other hand, have been shielded from U.S. exports by a high duty rate as well as a favorable exchange rate (Competitive Assessment, U.S.

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ITC, Page 8). Further, many Canadian manufacturers have the advantage of actually being closer to the major U.S. population centers than many major U.S. manufacturers (Competitive Assessment, U.S. ITC, Page 21).

In view of the similarities between our countries and the extent of furniture trade between the U.S. and Canada we view the current duty differential as unnecessary and disruptive. Canadian furniture in many cases offers serious competition to U.S. manufacturers. The same is true of U.S. furniture in Canada. Given the sound basis for that competition, neither country's furniture industry should be threatened by a removal of all duties or their equalization. Further, it is obvious that consumers in both countries would be well served by a reduction in duties and resulting reduction in furniture prices.

The AFMA believes the time has come to allow U.S. furniture manufacturers to compete with Canadian manufacturers on the same basis our domestic manufacturers compete with each other. The Congress, in passing trade negotiating authority for the U.S., evidently agreed with this direction for our international trade policy. To date, however, there have been no concrete results.

S. 1801/H.R. 3644 would promote more equitable competition between the U.S. and Canada on furniture products by moving to end the tariff disparity. The legislation would authorize free trade negotiations on furniture products between the U.S. and Canada. If a free trade agreement were not achieved, U.S. tariffs on furniture products would be gradually increased until they were at a level equal to the Canadian tariff set for American furniture products. At no time would S. 1801/H.R. 3644 cause U.S. tariffs to rise above the Canadian tariffs. The goal of the Fair Furniture Trade Act is free trade on furniture products with Canada, a step that would benefit manufacturers, retailers, and consumers in both countries.

Conclusion

The furniture industry, in recent years, has become more international in scope. Reflected both by inroads made by imported furniture into markets traditionally dominated by the U.S. furniture industry and by U.S. companies expanding their horizons overseas in search of new markets, the impact of trade-related policies cannot be overstated.

The behavior of the U.S. Government in the area of furniture trade has been exemplary: the U.S. has consistently lowered its effective tariffs on furniture over the past two decades through outright reductions, through the extension of very favorable tariff treatment to certain countries, and through its provision of duty-free status to certain developing countries -- even where those countries have become major international competitors in furniture (and other) trade.

However well-meaning these efforts are, they carry with them one fatal flaw. As practiced over the past two decades, with respect to the American furniture industry, the "free trade" and "lowered tariff" thrust of our government's trade policy has been too one-sided. U.S. backed agreements and Congressionally approved programs have hampered the ability of the U.S. furniture industry to compete in its own marketplace. They have also led to a partial restructuring of this industry not based upon the free flow of trade in international commerce. And all of this is occurring during a period predicted to be the "Golden Age of U.S. Furniture Manufacturing."

AFMA urges the Senate Finance Committee not to disapprove the Administration's request for authority to enter into bilateral trade negotiations with Canada, and strongly supports a free trade agreement on as broad a basis as possible. In addition, AFMA strongly supports the Fair Furniture Trade Act as a means of ensuring that our exports are accorded equitable treatment with regard to the Canadian market.

STATEMENT OF LAWRENCE A. FOX, VICE PRESIDENT, INTERNATIONAL ECONOMIC AFFAIRS, THE NATIONAL ASSOCIATION OF MANUFACTURERS, WASHINGTON, DC

Mr. Fox. Thank you, Mr. Chairman. In the interest of time, I will speed this up as much as I can.

The Chairman. Your entire statement will be in the record, as will Mr. McMinn's and Ms. Sloan's also.

Mr. Fox. Thank you. The American manufacturers have an enormous stake in the successful negotiation of an expanded trade agreement with Canada, whether it is called free trade or something else. The board of directors of NAM 2 months ago unanimously approved a broad-scale negotiation with Canada and established the proviso that such a negotiation could take place and could be approved, only if it met the economic interests of the United States; and we think that it is possible that may be done.

We believe a fast-track negotiating approach is consistent with the objectives of obtaining a good deal for the United States, and we think it is possible for this committee and the Ways and Means Committee to develop a system of consultation with the U.S. Trade Representative so that you are kept informed on the progress of each of the major issues so that, when the negotiation is concluded, it is one that has met your desiderata or the agreement would not be presented.

In a sense, NAM has approved the approach for the negotiation on the same basis; that is, we would be presenting to the administration our views and the views of our members in the course of negotiation. We believe that the United States is fully competitive, that it is anomalous, that Canada should have a $22 billion trade surplus with us. We believe that part of the problem, frankly, is Canadian Government interventionism and Canadian Government protectionism. We think this is a unique—and I would go with the word "historic"—opportunity to really achieve a level playing field with Canada, and we ought not to lose that opportunity.

We think the agreement should cover everything that affects trade: Tariffs, nontariff barriers, investment controls, intellectual property rights, and in a special way, exchange rates, as I will allude to in a moment.

We believe that the Canadian emphasis on secure market access to the United States and the reference to what they call "contingency protection"—I find that personally an obnoxious term—is a misused expression. I think there are protectionist elements on both sides, and the purpose of the agreement should be eliminate as many of those as possible at all levels of government, both Federal and Provincial and certainly on the State side in the United States.

We don't believe that any one issue should be determinative of the outcome, and certainly the whole negotiation should not be held back for any one issue; but we think that current trade disputes should be settled promptly. From the manufacturing standpoint, one of the issues that we have in mind is the pharmaceutical provision in Canada which, in fact, requires that American pharmaceutical manufacturers give up property rights in order to permit mandatory licensing of their production rights to generic firms in Canada as a condition to establish markets in Canada.

That is what I would call a banana republic kind of trick, and Canada ought to be required to give that up. We believe that the address of investment issues is important because we have learned that through the manipulation of the conditions of admission of investment, trade flows are affected. The previous experience with Canada under their Foreign Investment Review Agency [FIRA] reveals that, although conditions are somewhat better under "Investment Canada," we would like to see all of the Canadian investment controls eliminated.

Finally, I wanted to express two desiderata. On the exchange rate, I heard Ambassador Yeutter say that it has caused virtually the whole trade deficit. I am not sure that is the case; but if it is that important, then we have to have a provision in the trade agreement for consultation with regard to the exchange rate. I wouldn't go beyond that now because we can't design at this time what that exchange rate provision should be; but I am confident that a negotiation cannot ignore the exchange rate. The Canadian Manufacturers Association, in endorsing the negotiation, has an exchange rate provision in their proposal to the Canadian Government.

Finally, I would conclude that there ought to be some sort of joint commission to settle trade disputes. We now have a perfect setup for disputes going on forever and not being settled. I think the trade agreement should have a dispute settlement mechanism and a commission to deal with problems before they get out of hand and become generational in nature. Thank you.

The CHAIRMAN. Thank you. I will insert a statement of Senator McClure's after the opening statement.

[The prepared written statement of Mr. Fox follows:]

TESTIMONY OF THE NATIONAL ASSOCIATION OF MANUFACTURERS

BY

LAWRENCE A. FOX

ON

U.S.-CANADA TRADE NEGOTIATIONS

BEFORE THE COMMITTEE ON FINANCE

OF THE UNITED STATES SENATE

APRIL 11, 1986

Mr. Chairman, Members of the Committee, I am Lawrence A. Fox, Vice President for International Economic Affairs of the National Association of Manufacturers. We understand, Mr. Chairman that one option open to the Finance Committee on the question of the prospective bilateral trade negotiations with Canada was to do nothing. That is the Book-of-the-Month Club option: Don't do a thing. The book and the bill will come in due course. The issue of a new trade agreement with Canada is too important for that, Mr. Chairman. NAM commends you for calling these hearings, and we are grateful for the opportunity to express our views on this issue.

The National Association of Manufacturers, founded in 1895, is the oldest national trade association. At present, we have over 13,000 members, and collectively they represent about 80 percent of U.S. industrial output. Their employees make up roughly 85 percent of U.S. industrial employment.

My purpose today is to discuss U.S.-Canada trade, not the larger issue of U.S. trade and competitiveness. I would note, however, that in 1985 the U.S. deficit in manufactured goods alone, $114 billion, was equal to 76 percent of the total trade deficit of almost $150 billion. Manufactures account for 71 percent of U.S. imports, for 68 percent of our exports globally, and for about 85 percent of our exports to Canada. The stake of American industry in any trade negotiation, therefore, is enormous.

NAM RESOLUTION

I have included as part of my statement the NAM Resolution on U.S.-Canada Trade, which was approved unanimously by our board of directors in February. This states that, "The National Association of Manufacturers supports the proposal for U.S.-Canadian bilateral trade negotiations," and through it the NAM "urges the Administration and the Congress to move forward toward a new framework for the U.S.-Canadian economic relationship." It gives our reasons for believing that there are advantages to be gained for U.S. industry, and it expresses some of our caveats and concerns.

An economic consultant in Ottawa has dubbed the proposed free-trade-area talks the BETA negotiations, for Bilateral

NAM

ADOPTED BY NAM BOARD OF DIRECTORS
FEBRUARY 7, 1986

NAM STATEMENT ON U.S.-CANADA TRADE

The National Association of Manufacturers appreciates that American economic relations with Canada are different in several important respects from our economic relations with other countries. Canada is America's largest foreign customer, our principal foreign supplier, and the recipient of more U.S. investment than any other country. Because it is spread across a continent, U.S.-Canadian trade is as much a series of regional phenomena as it is a relationship between two separate nations.

The very closeness of our economic cooperation has created a situation in which government interference with the markets of the two countries can be a greater cause for concern for both American and Canadian businesses than in other economic relationships.

For these reasons and because of the potential for building on the existing high level of business cooperation between our two countries, the National Association of Manufacturers supports the proposal for U.S.-Canadian bilateral trade negotiations.

Any agreement resulting from these negotiations should advance the economic interests of American industry. The opportunities to do so are numerous. They include tariff reductions, meaningful reductions in Canadian federal and provincial subsidies, reductions in Canadian federal and provincial non-tariff barriers, enhanced protection for intellectual property rights, and agreed limits over the Canadian government's ability to restrict and/or control U.S. investment in Canada. In addition, an effective and expedited disputes settlement procedure should be obtained, as well as an agreed procedure for consultations regarding the exchange rate between the Canadian and U.S. dollar so that trade distortions arising from this cause can be resolved. The NAM believes that success in these areas is likely only if the U.S. Government accords significant weight to the advice it receives from the U.S. private sector in the course of the negotiations. If these goals are not substantially achieved, NAM will not be able to support a new trade agreement with Canada.

Because of the importance of securing an agreement that advances U.S. economic interests, the U.S. Trade Representative should include as part of the Administration's explanation of the agreement a clear statement of the agreement's expected economic impact on U.S. interests when the time comes for an agreement to be submitted to the Congress.

NAM believes that the resolution of existing disputes between the United States and Canada should be given a high priority. The sooner these matters can be cleared from the U.S.-Canadian agenda of commercial issues, the greater the likelihood that a trade enhancement agreement benefical to both countries can be negotiated.

In the hope that such an accord can be achieved, the National Association of Manufacturers urges the Administration and the Congress to move forward toward a new framework for the U.S.-Canadian economic relationship.

-NAM-

Enhanced-Trade Agreement. By whatever name, the impetus for these negotiations seems to derive from two quite different strains in Canadian thinking. On the one hand, Canada seeks to assure her producers of even more secure access to the U.S. market. On the other, government officials and others in Canada believe that the discipline of more open trade with the United States will help foster a family of more competitive Canadian industries. Put in terms of simple metaphores, Canadians want to give their exporting industries the warm milk of secure access, and they want to administer a cold, sobering but invigorating, shower to the Canadian industrial economy as a whole.

Our response to the proposal for free-trade-area negotiations can draw from these ideas, but it has to begin with this question: Why is it that the United States has a $22 billion trade deficit with a country that is, in many respects, less competitive?

National economies are complex phenomena, and there are a number of reasons for this anomaly. Certainly one reason is the current web of Canadian protectionism. The U.S. furniture industry presents an excellent illustration of this problem, and it is unfortunately only one of many. Illinois printers who face discriminatory postal rates in Canada and a tariff of over 30 percent on catalogues to Canada offer another; Alabama producers of insect screening another; and U.S. brewers and wine makers another. Dismantling that protectionism should be a boon to both the U.S. and Canadian economies. It will help redirect Canadian resources to their most productive industries, and it ought to give U.S. producers a better chance to reap the export earnings that their productivity should have earned them. Additionally, it should enable companies with facilities on both sides of the U.S.-Canadian border to rationalize their production facilities. That too can only be in the interest of both the United States and Canada.

But what of Canada's desire to enhance her security of access to the U.S. market? NAM agrees with the general position expressed by U.S. Administration officials that everything should be on the table. At the same time, we think it is important not to be confused by Canadian rhetoric. Their officials complain about our contingency protection. As Table 1 below illustrates Canada's trade surplus with the United States has been increasing steadily at least since 1977, and it is now second only to our deficit with Japan. That is hardly evidence of protectionism.

Further, when we examine the phrase "contingency protection", we find that the "contingencies" in question are generally unfair trading practices that hurt U.S. industries and the "protection" is the use of GATT sanctioned responses to those practices. Of course we should talk about these issues. In the context of a wholly new arrangement for U.S.-Canada trade, it may be that changes in their laws and ours will make sense that do not make

TABLE 1

U.S. TRADE WITH CANADA
1977-1985

	Exports	Imports	Balance
1977	25.0	30.6	- 5.6
1978	27.6	34.6	- 7.0
1979	32.2	39.0	- 6.9
1980	35.4	42.0	- 6.6
1981	39.6	46.8	- 7.6
1982	33.7	46.8	-13.1
1983	38.2	52.5	-14.3
1984	46.5	66.5	-20.0
1985	47.3	69.4	-22.1

Source: U.S. Department of Commerce, *Highlights of U.S. Export and Import Trade*, 1977-1983. Imports c.i.f.

sense when considered in isolation. Nevertheless, Canada should not pin her hopes or her negotiating strategy on revolutionizing or undermining the U.S. unfair trade statutes.

OUTSTANDING ISSUES

As stated in our resolution:

> NAM believes that the resolution of existing disputes between the United States and Canada should be given a high priority. The sooner these matters can be cleared from the U.S.-Canada agenda of commercial issues, the greater the likelihood that a trade enhancement agreement beneficial to both parties can be negotiated.

It is not necessary to rehearse these issues. Both sides know what they are, and it is not our belief that general negotiations should be held hostage to any one issue.

Yet there is one, I think, that has become especially important. This is the pharmaceutical issue. From the U.S. perspective, it embodies high economic stakes, an important commercial principle, and the ability of each partner to rely on the good faith of the other.

Canada is not the only country in the world in which the bulk of medical costs are borne by the public sector. Indeed, the United States is probably the only major industrial country where this is not the case. Yet Canada is alone among industrial countries in its policy of using compulsory licensing of new drugs as a way of controlling medical costs. This seems to us a bad policy for Canada, as it effectively discourages anyone who might otherwise invest in pharmaceutical research and development in Canada.

Compulsory licensing is certainly a bad principle as far as the NAM is concerned. We believe that the future of open international trade depends upon building strong protections for intellectual property rights into the international trading system. Compulsory licensing flies in the face of that effort. Finally, this issue is critical because it touches on issues of trust. The U.S. government has received repeated assurances that Canada's present compulsory licensing law, Section 41 of the Canadian patent law, would be amended. It hasn't happened yet. If the Canadian government's promise to modify their compulsory licensing program is not quickly redeemed, the issue could cast a cloud over the proposed bilateral trade negotiations and dim chances for success in this effort.

NEGOTIATIONS

As to the issues which are widely expected to be part of the negotiations, it is perhaps too early to set out precise objectives. There is still a great deal to be learned. Most of the broad areas for negotiation have been identified by one side or the other, and we do not need to dwell on them at this time. There are three, however, which need to be emphasized more than they have been.

Investment. The first is investment. It is odd to us that the Canadian Trade Negotiations Office (TNO), which has been set up under Simon Riesman to handle these negotiations, has teams working on tariffs, trade in services, government procurement, and other topics, but none on investment. This is not an oversight. We have heard Canadian officials argue that there is no need for investment issues to be included in these negotiations. They are wrong. And the National Association of Manufacturers would strongly oppose any trade agreement with Canada that did not include meaningful investment provisions.

It is ironic that Canada should object to including investment in light of the important role investment policy has already played in bringing us to this juncture. The United States and Canada are not only each other's largest trading partner; each is the other's largest investment partner as well. U.S. investment in Canada is about $90 billion and Canadian investment in the United States is about $30 billion. Yet, as you know, Mr. Chairman, Canadian investment policies, specifically the policies of the now defunct Foreign Investment Review Agency, have been among the most contentious issues in recent years between the United States and Canada. Many of these policies have been trade distorting, and some have been found to be in violation of the GATT. Canada's well publicized movement away from the policies and attitudes of FIRA -- its establishment and promotion of the FIRA replacement Investment Canada -- are among the developments that have given credibility to the idea of a free-trade-area.

It would be foolish for the United States to enter a major agreement with Canada without incorporating into that agreement the investment conditions that make it possible. In saying this, I am not necessarily expressing the view that the move from FIRA to Investment Canada has by itself created those conditions, but certainly it has been a step in the right direction.

A further irony in Canada's reluctance to discuss investment policies in the context of the trade talks is that she is clearly selling investment in Canada on the basis of Canada's good trading relationship with the United States and the prospect of an even better one. Investment Canada has offices in New York, Chicago, Los Angeles, London, Paris, Bonn and Tokyo, and their message is this. Put your North American plant in Canada and reap the advantages of a market of 250 million people. We have no quarrel with that, but the investment must be free and unrestrained.

Exchange Rates. Another difficult issue that should form part of a trade agreement between the United States and Canada is the question of the exchange rate between the U.S. and Canadian dollars. If we have learned anything in the last five years it is that serious misalignments in exchange rates can make a mockery of the best trading arrangement. It should be obvious that a free-trade-area accord with Canada should include, as a matter of course, a consultation mechanism for dealing with potential problems in the exchange rate relationship between the two dollars.

Dispute Settlement. Canadian official frequently express the view that there would have to be an international, U.S.-Canada dispute settlement body establishment to make a major new agreement work. We agree. We favor a bilateral dispute settlement procedure which will solve problems rather than perpetuate disputes--possibly by means of a standing joint commission.

CONCLUSION

A lot is made of the disparity in size between the United States and Canada and the fact that these negotiations loom larger in Canadian politics today than they do in our own. There is the impression that this is an enormously important question for Canada but just a ho-hum issue for the United States.

That impression may serve Canadian negotiators, but it could not be more inaccurate. Our 1985, $150 billion trade deficit is the inescapable evidence that there is a crisis in American trade and American competitiveness. Our country cannot afford any more big mistakes in trade. We cannot afford to miss an opportunity to increase our exports or to make our factories more efficient and more competitive. And we cannot afford a trade deal with our largest trading partner that does not advance the interests of U.S. industry.

NAM's hope, Mr. Chairman, is that this Committee will approve the Administration's plan to enter into bilateral negotiations with Canada. We believe an affirmative statement to this effect is desirable. We are sensitive to the fact that the requirements of the negotiating process itself impose limits on any such statement. To anticipate the compromises that one expects would undercut our negotiators, while too rigid a statement of Congressional requirements might preclude the compromises that will be essential to a good agreement. What the Committee can and should do, we believe, is to reinforce the position that a trade agreement with Canada must advance the economic interest of U.S. industry or it will not be approved.

I said at the outset, Mr. Chairman, that we regard this as an important hearing. More important still, of course, will be the hearing I hope you will be able to call in 18 months, or two years, when the question will be: How should Congress vote on the new trade agreement with Canada. We would like to testify at that hearing too. I hope we will be testifying in favor of the agreement, but that will depend on the agreement itself.

Thank you.

STATEMENT OF LUCY SLOAN, EXECUTIVE DIRECTOR, NATIONAL FEDERATION OF FISHERMEN; AND MEMBER, BOARD OF DIRECTORS, NORTH ATLANTIC FISHERIES TASK FORCE, WASHINGTON, DC

Ms. SLOAN. Thank you, Mr. Chairman. I am delighted and comforted by the committee's concern to ensure us that you will be involved in this process because, with Ambassador Yeutter's statement that of course there will be some tradeoffs, there will be some winners and some losers, but that he wants everything on the table, as you and Senator Chafee and Senator Mitchell, historically the fisheries trade relationship with Canada has been a horse and rabbit stew; and the United States has always been the rabbit.

And for that reason at least, we would be very concerned that, if the agreement were to go forward, we would like to ensure that fisheries be taken out of it. Fisheries is the only product that is a migratory natural resource, the management of which has a significant impact on what is available in the marketplace.

We have been very concerned because the United States management philosophy and the Canadian management philosophy are about as different as they could be. The problem with the Canadian provinces' subsidies is one of the difficulties that we have had in the five actions before the one in which we are currently involved before the ITC have caused. As a result, although I think that it may very well be the case, as Ambassador Yeutter has suggested, that we would be looking at 6-inch headlines as a result of today's testimony, I think that the 12-inch headlines that would result if the Congress were to turn down the free trade agreement after it had been negotiated are probably quite accurate because, even when the United States turned down the 1979 United States-Canadian East Coast Fisheries Agreement, we were told that there were 12-inch headlines in Canada; and as a result of that, we would strongly urge to avoid a duplication of the problems that ensued when we turned down the 1979 agreement.

The fisheries, because it is a transnational migratory natural resource, should be excluded from a free trade bilateral. We are not saying we are not willing to have some sort of fisheries discussions, but to do so in a situation where our chief negotiator says, of course, there will be some tradeoffs, we are very much afraid that the U.S. fishing industry might be one of the things traded off. Thank you.

Senator BENTSEN. Thank you very much. Are there any questions of the witnesses? Oh, excuse me, Mr. McMinn, you have not testified. I am sorry.

[The prepared written statement of Ms. Sloan follows:]

11 April 1986

national federation of fishermen
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NORTH ATLANTIC FISHERIES TASK FORCE
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GLOUCESTER, MASSACHUSETTS 01930
(617) 281-4818

US--Canada Free Trade Negotiations

We strongly urge that fisheries not be included in the President's proposed bilateral negotiations between the United States and Canada on a comprehensive free trade arrangment.

We are not suggesting that bilateral discussions at appropriate times not take place. Rather, we are concerned that because, between the United States and Canada, fisheries trade is inextricably interwoven with fisheries management, neither trade nor management would be properly served by dealing with fish in a forum which was not designed to take into consideration the importance of the variables inherent to a migratory natural resource whose ultimate destination was the marketplace.

A recent internal draft National Marine Fisheries Service document points out as regards our fisheries trade relationship with Canada, "This bilateral relationship is obviously more important within the limited context of fisheries than it is in the context of our general bilateral merchandise trade."

In fisheries management, not only are we dealing with fisheries stocks both transboundary and straddling, but also with two entirely different management philosophies with widely different degrees of government intervention.

Given the interwoven and specialized nature of fisheries trade with fisheries management, we respectfully request that when your Ctte makes its finding on the President's US--Canada free trade bilateral initiative, you include as well a finding that fisheries should be omitted from the range of products to be considered.

* * *

11 April 1986

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Testimony before
SENATE CTTE ON FINANCE
on
US--Canada Free Trade Negotiations

Good morning, Mr. Chairman, Senators. I'm Lucy Sloan, Executive Director of the National Federation of Fishermen and a Member, Board of Directors, North Atlantic Fisheries Task Force. NFF is the only national organization representing coastal commercial fishermen. NAFTF is an industry group established to study the US North Atlantic fishing industry's trading relationship with other countries and actively to seek solutions to trade and related problems.

We strongly urge that fisheries not be included in the President's proposed bilateral negotiations between the United States and Canada on a comprehensive free trade arrangment.

We are not suggesting that bilateral discussions at appropriate times not take place. Rather, we are concerned that because, between the United States and Canada, fisheries trade is inextricably interwoven with fisheries management, neither trade nor management would be properly served by dealing with fish in a forum which was not designed to take into consideration the importance of the variables inherent to a migratory natural resource whose ultimate destination was the marketplace.

After all, as an internal draft National Marine Fisheries Service document points out, "The amount of trade involved is not a critical portion of our total bilateral merchandise trade, which totalled $45 billion in US exports to Canada, and $66 billion in Canadian exports to the US in 1984. Of this, bilateral seafood trade accounted for $121 million in US sales to Canada, and $788 million in Canadian sales to the United States....the United States...receive[d] about 62 percent of all Canada's seafood exports in 1984, about 53 percent of all US seafood imports. Our exports to Canada represent 14 percent of all US seafood exports. This bilateral relationship

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Counsel and Washington Representative
[illegible]

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is obviously more important within the limited context of fisheries than it is in the context of our general bilateral merchandise trade." [Emphasis added.]

As regards fisheries management, not only are we dealing with fisheries stocks both transboundary (that is, migrating between exclusive economic zones) and straddling (migrating between EEZs and the adjacent areas beyond 200 miles), but we are as well dealing with two entirely different philosophies of fisheries management.

In the United States, we have sought, wherever possible, to optimize production of this food resource while ensuring both maximum flexibility for fishermen to move among fisheries and only minimum government regulatory intervention to assure adequate conservation and management under the Magnuson Fishery Conservation and Management Act.

In Canada, on the other hand, the governments--federal and provincial--for political reasons fueled by economics, are substantially involved in the Canadian fishing industry at all levels, even to the point of creating crown corporations and super companies, the latter with government equity infusions.

These quite different levels of government involvement in management and, in the case of Canada, operations, manifest themselves in the United States' competitive disadvantages in both the US and third country markets.

Further, I understand that through the National Governors' Association, the states have raised the concern that they have a strong advisory role in any negotiations that involve Canada. In fisheries management, the states--and the provinces--have important regulatory responsibilities. Neither the states nor the provinces always agree among themselves on how to resolve complex fisheries problems, problems which often may have direct and significant impacts on the amounts of fisheries products and their relative costs in the volatile and specialized marketplaces.

BEST COPY AVAILABLE

Thus, given the interwoven and specialised nature of fisheries trade with fisheries management, we respectfully request that when your Ctte makes its finding on the President's US--Canada free trade bilateral initiative, you include as well a finding that fisheries should be omitted from the range of products to be considered.

Thank you.

Dear Mr. Chairman,

7 April 1986

Our differences with Canada--the results of differences in government involvement in fisheries management and fisheries in the marketplace--are long-standing, as this brief testimony indicates. I would request that it be made a part of the record with my testimony for 11 April.

Thank you,
Lucy Sloan

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Oversight hearing
on
Fishery Imports and Their Importance
To the United States Fishing Industry
SCtte on Fisheries and Wildlife
Ctte on Merchant Marine and Fisheries
17 May 1984

Good morning, Mr. Chairman, Members. I'm Lucy Sloan, Executive Director, National Federation of Fishermen. We are a Federation of organizations, and through our member groups, we represent fishermen who fish from the Gulf of Maine to the Gulf of Mexico and from California to Alaska and the Central Pacific. Among the species our members catch are traditional and less utilised finfish, crab, albacore tuna, shrimp, swordfish, lobsters, eels, clams, and oysters.

The United States is, we're told, one of the best growth markets for seafood in the world. Fisheries is an international industry. And seafood is an international market commodity.

Consider those statements in light of all the fisheries development rhetoric we've heard for the last decade. There's no question that general awareness of seafood and the industry which produces it in this country have improved significantly in the last eight years. You in Congress have been the primary vehicle we've had to do this, and we really appreciate it. Your hearing today is an example. And recently, the Executive branch has also become increasingly involved in working with us to realise the potential of the Fishery Conservation and Management Act, including its amendments.

Nonetheless, the United States industry remains at a significant disadvantage, largely because of the striking differences among how other nations see their fishing industries (indeed, all of their industries) and how our government sees ours. The United States prides itself on being a so-called free trade nation in a world in which free trade is an increasingly endangered species. We have said repeatedly that we do not wish to be subsidised as other fishing industries are around the world, or even as the United States farmers are. We continue to think that these massive programs would undermine the basic reasons for which so many of our people go fishing. But it is hardly fair for our government to tell us to "get out there and compete" when our major competitors are considerably more heavily involved with their respective governments than are we. Canada, Iceland, Norway, and Japan are all examples of this involvement, with a wide range of programs among them. Jake Dykstra summed up our frustrations in trying to deal with this problem when he responded to Ian Hamilton, Canadian Consul and Trade Commissioner's plea for US "cooperation" in the US marketplace--where "cooperation" would really mean US acceptance of the role of rabbit in the horse and rabbit stew that the Canadian market in the United States increasingly is becoming. Jake said, "When Ian says we [the US and Canada] should walk into the sunset hand-in-hand, my answer is 'Get off my foot and we will.'"

Canada, with its Kirby and Pearse Reports, is the most immediate example we have on both coasts to demonstrate the impact which galloping government involvement in one country's seafood industry has on the fishing industry of the United States. Jim Salisbury, Maine Fishermen's Cooperative Association, and Joe Easley, Oregon Trawl Commission are here today to discuss the impact on our markets Canada and other nations do have.

As you listen to them, recall how many times before we've discussed variations on this theme with you. How can my fishermen be expected to swallow the rhetoric about the US as a free trade nation and the opportunities for fisheries development and our responsibilities to get out there and compete when they still pay significant duties and/or tariffs on twine, nets, and electronics on the one hand and must fight for niches in a marketplace where heavily government subsidized products from other major fishing nations compete with the virtually unsubsidized fish which they produce on the other ?!

We think that a much clearer understanding of the substantial differences between the United States government's attitude toward our fishermen and other nations' attitudes toward is essential. Until we achieve in our government officials a working awareness of the specific impacts of per/pound subsidies, vessel building and operational subsidies, subsidized shoreside installations, for example, which other countries provide, we will never fully understand how best to deal with those impacts in our domestic marketplace--the marketplace which many knowledgeable people think is the best chance for market expansion of several US-caught and processed seafood products.

We need tariffs and countervailing duties. The International Trade Commission's Northeast investigation, which Senator Cohen has worked with Jim and others in New England to get, is a very important step, and we certainly appreciate the work the Senator and his colleagues in the New England delegation have put into it. It is the fifth time in the decade I've been working for fishermen we've tried to deal with the problem of Canadian imports. We are much better prepared this time and we are working together to try to achieve the success we so badly need, but we may need to come to you at some point for additional assistance to achieve these tariffs and duties nationwide.

Thanks very much for your continuing interest. We really appreciate it!

STATEMENT OF ROBERT W. McMINN, SENIOR VICE PRESIDENT, PLANNING/DEVELOPMENT, AUTOMOTIVE PARTS & ACCESSORIES ASSOCIATION, LANHAM, MD

Mr. McMINN. Thank you, Mr. Chairman, members of the committee. I am Robert McMinn, senior vice president of the Automotive Parts & Accessories Association. APAA represents 1,700 members who manufacture and sell automotive parts and accessories. Many of our 950 manufacturer members sell to both the vehicle assemby or original equipment markets and to the replacement markets; but the lion's share of their profits are made in the aftermarket.

Our industry is a major contributor to this country's economy, providing twice as many jobs as the carmaking segment. We also are a major exporter, $13.7 billion in 1985; $9.8 billion of that was business done with Canada.

Mr. Chairman, we are here today to ask you and the committee to urge our negotiators to keep automotive aftermarket tradeoff on the bilateral bargaining table. Free trade requires open and fair trade practices. We have this in part with Canada, but not with the unintended third parties which would benefit most from the proposed new agreement. We are referring to the Japanese and Korean firms which are responding to Canada's aggressive program to locate plants there. Initially, these plants would provide the parts used in assembling cars, both in Canada and the United States.

Under the auto pact, these parts and cars cross the border duty free, although with the mood of the committee today, we may not have an auto pact by the end of the day. [Laughter.]

Mr. McMINN. Once in production, though, they will turn to the lucrative aftermarket. But since Canada's aftermarket is less than one-tenth of the $100 billion United States market, it is obvious where the majority of these aftermarket products will be shipped. The present aftermarket duties of 4 to 6 percent for parts entering the United States provide a small but necessary protection for our domestic suppliers.

If eliminated under a bilateral agreement, Japanese manufacturers located in Canada could bank those fees as pure profit. If the issue were solely between Canada and the United States, it could be viewed in a different light. However, both of our countries are threatened by Japanese barriers that thwart our sales to them and to the other markets that they have come to dominate.

Our responses to that threat differ. As an illustration, Canada and the United States both had the only foreign pavillions at last fall's Tokyo motor show. While our firms were trying to sell United States made products, the Canadians were selling Ontario real estate, and they have been successful. They have got plant commitments from Honda, Toyota, Suzuki, and a host of supplier companies. Korea's Hyundai also has announced plans for both assembly and parts plants in Canada.

We don't shrink from healthy competition, but we do object to having the playing field tipped to the advantage of Canada and its Japanese transplants. Elimination of the aftermarket tariffs would add to the price advantage already enjoyed by Canada through exchange rates and labor cost differences. This combination would make it very easy for the Japanese manufacturers to defuse our concern over the worsening trade balance by transferring production to Canada, reducing the surplus between Japan and the United States, replacing it with an additional surplus between Canada and the United States.

In either case, the ultimate winner is Japan.

Our views are well known to Ambassador Yeutter, and he linked us into the talks as an adviser through one of his industry sector committees. But, the most important voices now are yours, Mr. Chairman, and those of your committee. We ask that you urge our negotiators to exclude automotive after-market trade from the agreement and allow us to retain the minimal protection offered by the present tariffs.

We have given the staff a much more detailed analysis of the issue, and we appreciate the opportunity to share our views with you. We would be happy to answer any questions.

Senator DANFORTH. Ladies and gentlemen, thank you very much.

[The prepared statements of Mr. McMinn and Senator McClure follow:]

STATEMENT OF
ROBERT W. McMINN
SENIOR VICE PRESIDENT OF
PLANNING/DEVELOPMENT
FOR THE

AUTOMOTIVE PARTS AND ACCESSORIES ASSOCIATION, INC.

PRESENTED TO
THE COMMITTEE ON FINANCE
UNITED STATES SENATE
APRIL 11, 1986
RE: U.S.-CANADA FREE TRADE AGREEMENT

Mr. Chairman and Members of the Committee:

I am Robert McMinn, Senior Vice President of Planning and Development for the Automotive Parts and Accessories Association (APAA). Thank you for the opportunity to meet with you today.

Mr. Chairman, we are here today to ask you and the committee to urge our negotiators to keep automotive aftermarket trade off of the bilateral bargaining table. Both Ambassador Yeutter and Secretary Baldrige learned our views early on, following Prime Minister Mulroney's September 26, 1985 proposal. We are pleased to say that Ambassador Yeutter has tapped us as advisors. APAA is largely playing that role through our president, Julian C. Morris, who serves on the Transportation Equipment Industry Sector Advisory Council (ISAC) 16.

APAA is a trade association located in Washington, D.C. Our association represents 950 manufacturers producing parts, accessories, tools, equipment and supplies for consumption in the Original Equipment Manufacturers (OEM) (car companies) and consumer markets. It is the consumer markets, the aftermarket, where our industry makes its greatest profits and where most of our members' products are sold. We have another 700 members engaged in selling, as members of the distribution chain, manufacturers' representatives, export management companies, and retailers.

The aftermarket is vital to the nation's economy. In fact, our financial health means more to America's economic well-being than even that of the OEM's. Not only do we have more companies -- some 40,000 firms engaged in automotive supply -- but we also have double the employment of the OEM's and their dealers. The automotive supplier industry also is essential to American military might, as demonstrated by past mobilization efforts. And, in the vital area of trading strength, our industry plays a key role. In 1985, industry firms exported $13.7 billion worth of parts and accessories, including $9.3 billion -- 70 percent of the total -- to Canada.

Given Canada's place as America's leading trade partner, it is understandable that the Macdonald Commission Report on Canada's economic future made the free trade proposal its centerpiece. We also recognize that the concept has many Administration and Congressional proponents who wish to eliminate tariff barriers between principal trading partners. We believe the proposal is worthy of the serious study undertaken by this committee, and we recognize that there are sure to be some industry sectors in both nations where a free trade agreement would prove mutually beneficial.

APAA does not believe that this would be the case for the automotive aftermarket industry. As inviting as "free trade" sounds to an industry whose survival hinges on gaining access to global original equipment (OE) and replacement parts markets, it takes a fair and open trade regime to make it work. We have this with Canada, but we do not have it with one unintended third party that would benefit by the agreement -- Japan -- and we may not have it with Korea and others that settle in Canada.

Japanese suppliers are heeding the siren call of Canadian government/industry investment enticements. Under a free trade regime, these Japanese firms would get a huge bonus: aftermarket exports launched duty-free from Canadian bases into America's $100 billion plus aftermarket. They could bank the average 4-6 percent duty savings as pure profit.

While the U.S. aftermarket is the major prize in world parts trade, Canada's aftermarket, while important, is but one-tenth the size of ours. On paper, the removal of their high 9-10 percent aftermarket tariff walls may look like a major break for U.S. exporters. But, if access to a smaller Canadian market must come at a cost to domestic market competitiveness by ending our minimal U.S. tariff protection, then it is too high of a price to pay. Were it truly trade between the two domestic industries, the issue could be viewed in a different context.

Both nations' parts industries have found their survival threatened by Japanese barriers that thwart OE sales and take a toll on aftermarket sales in North America, Japan, and in export markets dominated by Japan. However, the similarity ends there, now that Canada's response to the threat has shifted radically. I witnessed their new strategy at the Tokyo Motor Show last fall, where the U.S. and Canada had the only two foreign pavilions. While our firms tried to sell U.S. made products, Canada was selling Ontario real estate.

It is important to note that prior to this new approach, Canada had a longstanding commitment to gaining market access for its parts and accessories manufacturers. Concern for its supplier base spurred the 1975 implementation of a duty remission program for imported vehicles. The objective was to induce foreign based auto makers to buy Canadian content, by netting out the value of that content from the dutiable value of the car maker's shipments to Canada. The 10 percent plus Canadian tariff makes this a valuable incentive. (Copies of the statute and implementing regulation are attached as Appendices A and B).

In one spin-off of this program, Canada offered Volkswagen (VW) duty free importation of cars into Canada in exchange for their manufacture of parts in Canada for export to VW's U.S. assembly plants. That plan was cut short by the auto making depression and the deep plunge in VW's equipment demands.

Finally, Canada's 1983 Private Sector Task Force on the Motor Vehicle and Parts Industries named a domestic content requirement as the cornerstone of its recommendations to the federal government. The task force proposal effectively would broaden the Auto Pact content stipulations to apply to Japanese and other foreign vehicle producers who market cars in Canada.

U.S. AUTOMOTIVE PARTS TRADE POLICY

In the U.S.. APAA has worked with the Department of Commerce (DOC) and the Office of U.S. Trade Representative (USTR) to begin development of our own program for the aftermarket. While we have joined Administration ranks in denouncing domestic content as bad economics that would threaten both short-term and long-term industry vitality, we still hope to gain Congressional enactment of the Automotive Products Export Council (APEC)-developed Parts Purchase Incentive Plan, tailored after the Canadian duty remission program. (Copies of our Plan legislative draft and analysis are attached as Appendices C and D).

Our Plan would be the lever -- an economic incentive -- to pry open Japan's closed OEM's and spur U.S. export sales. During last year's Tokyo Motor Show, Patrick Lavelle, then president of the Automotive Parts Manufacturers Association of Canada, told The Japan Times that their strategy shifted gears because export efforts "were doomed to failure." The reason cited: Japanese auto makers' close ties to their supplier families barred market entry. We will not concede these institutional barriers as insurmountable. Rather, let us put our Plan to work, and we will press those Japanese car companies' self-interest buttons to lift those barriers.

We believe the Plan would create American jobs, equip vehicle imports with American content and set off a chain reaction of growth in aftermarket sales. The incentive to buy would be a dollar of credit against vehicle duty for each dollar of American product purchased by foreign based auto makers. The credit would be available against an auto maker's shipments to the U.S., regardless of whether the incoming cars bear the American content, opening new markets to our exports. Current "American Goods Returned" law follows the Canadian program's deduction approach, netting out U.S. content before applying the duty. But, unlike Canada, where a 10 percent automobile duty makes for significant savings, the U.S. automobile duty is only 2.5 percent. Instead of the incentive offered by current law, our credit approach puts a real economic incentive in front of the Japanese.

The linchpin of the U.S. parts program is the industry/government Japan Initiative to crack Japanese car company-controlled markets. Through the exchange of buying and selling missions, begun with the Japanese government sponsored parts purchasing mission to the 1985 APAA Show, and the creation of a bilateral Trade Facilitation Committee (TFC) to help smooth the rough edges in private contract talks, we have a program to build American supplier opportunities wherever Japan builds and sells cars. This market opening campaign is on the move today, literally, with 12 American suppliers concluding a week long executive level selling mission to Japan's nine OEM's. The first TFC meeting takes place today, chaired by high level negotiators from DOC and the Ministry of International Trade and Industry (MITI).

Having looked briefly at the policy objectives of Canada and the U.S., we find a fundamental difference. In summary, it is Canadian industry support of domestic content versus the U.S. industry/government market opening initiative, preferably assisted by the leverage that our Parts Purchase Incentive Plan would provide. The bottom line is the same, however, as both industries work feverishly to develop new customers -- namely Japanese car makers -- to supplant the sagging parts demand of traditional Big Four customers.

While we have no quarrel with healthy competition, we must object to the playing field being tipped to Canada's advantage. We cite the well-reported Canadian government bounties to lure new Japanese supplier investment to Canada. In fact, it was with Canadian government blessings that the newly founded Pacific Automotive Co-operation, Inc. embarked in 1984 on a zealous mission to stimulate both the Canadian and Japanese parts industries.

Staffed by Japanese auto executives and directed by officials of the Japanese Automobile Manufacturers Association (JAMA) and the Japan Auto Parts Industries Association (JAPIA), PAC is waging an ambitious campaign to entice Japanese suppliers to take some of the sting out of U.S. political frustration with the mounting parts trade deficit, by entering the U.S. through the back door.

What makes all of this even more threatening is PAC's push for Japanese suppliers to use Canada as a springboard to launch duty-free original equipment exports into both domestic and Japanese car assembly plants in the U.S. This duty-free treatment is guaranteed by the Automotive Products Trade Act of 1965 (APTA) and the special Auto Pact between the U.S. and Canada authorized by that Act. Briefly, it permits most motor vehicles and OE parts to cross between nations duty-free.

While this is not the forum to discuss the Auto Pact, a review of these recent Pact developments helps underscore our alarm with unintended third parties benefiting by the program, and forewarns of similar exploitaion of a free trade aftermarket agreement. I have attached as Appendix E a PAC press release that highlights their selling pitch including the very salient point of duty-free treatment. Perhaps this fits the letter of the Auto Pact, but it clearly does not conform with the spirit. Moreover, it seriously undermines our market opening initiatives. Yet, if we can find a silver lining in this new Canadian strategy, it is the red flag it raises against exposing our domestic aftermarket to the same danger.

But, Japan is reacting to political pressure from both countries. Its chief response is to move more of its vehicle production to North America. Reluctant to choose from U.S. suppliers who are capable of supplying the entire gamut of Japanese auto manufacturing needs, Japanese car makers prefer to establish their own supplier families nearby. Faced with U.S. industry resistance to a network of new plants setting up next door to underutilized

American plants, Japanese firms are finding PAC's sales pitch most appealing. Not only will Canada welcome their suppliers, but the Japanese can locate close enough to the U.S. assembly plants for just-in-time delivery. All is done duty free and in full compliance with the Auto Pact.

Obviously, Canada offers advantages beyond a receptive climate. The strong U.S. dollar, that has hampered our firms' access to foreign markets, becomes a potent club against us as our chief trading partner offers a built in 25 percent plus discount on every component and car shipped to the U.S.

Add to this the lure of government grants and lower operating costs in the key areas of wages, utilities, and materials, and it is easy to see that our parts trade deficit with Canada could mount swiftly as Japanese suppliers exploit the Auto Pact to sidestep U.S. political pressures. Even before any Japanese, Koreans or other transplants take appreciable advantage of the favored treatment, the bilateral trade figures are trending against us. As the statistical table, attached as Appendix F shows, the U.S.-Canada parts trade surplus has shrunk from $2.2 billion in 1981 to $1.0 billion in 1984 and to only $500 million last year. And, our deficit in car trade has pyramided from $1.1 billion in 1981 to $5.5 billion in 1985.

It is imperative that we not aid this onslaught by making our aftermarket industry more vulnerable. Even with the status quo, we know that Japanese suppliers to American OE markets will enter our aftermarket with the same competitive advantages cited above. Moreover, their OE production base will help lower the cost of the extra units produced for the U.S. aftermarket, making their price competitiveness even more formidable.

In conclusion, Mr. Chairman, APAA beleives that our minimal aftermarket tariffs must remain intact to absorb some of the shock of the price advantage that the exchange rate alone guarantees. Elimination of these tariffs could set off a chain reaction of declining competitiveness at home, lower output, job losses and more off-shore sourcing. Moreover, our industry/government Japan market opening campaign will be undermined if we allow a Japanese sleight of hand that cuts their parts surplus with the U.S. by eating into our already reduced parts trade surplus with Canada.

Our views are well known to Ambassador Yeutter. But, the most important voices needed now are yours, Mr. Chairman, and those of the committee members, directing our negotiating team to exclude automotive aftermarket trade from the agreement, and to focus instead on sectors where benefits would be mutual.

The U.S. and Canadian auto making and supplier industries are so integrated that our General Agreement on Tariffs and Trade (GATT) partners have for 21 years permitted us to enjoy bilateral duty privileges which are denied them. As common as is our evolution so is the threat posed by foreign firms and governments that deny the market access available in North America. Where our countries develop policies for responding to that threat, we urge that the U.S. adopt the best of Canada's program, especially through prompt Congressional enactment of our Parts Purchase Incentive Plan. And, we must oppose policies inimical to American supplier industry interests. Once we have stopped the immediate threat posed to our aftermarket by the free trade proposal, we can move to explore the balance of our automotive trade relationship and determine what, if any, common interests we wish to pursue.

We appreciate this opportunity to share our views and would be happy to answer any questions you may have.

Apendices A to F are in the offical committee files

James A. McClure

STATEMENT OF SENATOR JAMES A. McCLURE
SENATE COMMITTEE ON FINANCE

APRIL 11, 1986

Mr. Chairman, I first wish to thank you for allowing me the opportunity to once again express my great concern about the devastating effect of Canadian lumber exports on the U.S. forest products industry.

Prime Minister Mulroney returned home after his recent meetings here in Washington with both Congressional members and the President and delivered a loud and clear message to the Canadian Parliament. His message was that there would be no preconditions to the start of free trade talks.

The Senate Finance Committee is now at a point where it must make a hard decision. You can either disapprove the "fast-track" procedure, or take no action, thereby granting tacit approval of the Administration's request. Should you choose the latter option, we will then have no choice but to rely on the judgements of the Administration and to trust that they will make good on their promise to resolve the timber crisis before the expanded talks begin.

The Administration has given us their word that they would deal with this problem before beginning any free trade talks with the Canadians. We now find ourselves in what I consider to be an extremely precarious predicament. Let me explain.

The Administration must now choose between our concerns and those of the Canadians. If the Prime Minister is to be taken at his word, then we must assume he is unwilling to resolve this problem before proceeding with free trade talks.

I understand that there are many more issues involved, but the Canadians must recognize that we are serious. We have tried to get the attention of the Canadians with threats of legislation. I am convinced if the timber issue is not resolved and the negotiations begin that the Senate will have no choice but to turn to a legislative solution.

The Committee's consideration may be the final opportunity to provide needed relief from the growing Canadian market intrusion. It may be our last opportunity to demonstrate to the thousands of families across this nation that depend upon the forest products industry for their livelihood that we place their welfare ahead of that of Canada. They are the ones that are paying the price for this blatant misuse of our free trade policies; not the Canadians.

If we do not act to deny the Administration's request, we play into the hands of the Canadians on this issue. I would suggest that it is going to be extremely difficult, if not impossible, for us to regain the attention of the Canadian government on this matter, if it is approved.

Before you make your final decision, I hope that you will carefully weigh the risks. Approval of the Administration's request will imply your total trust in their judgement on this issue. The economic well-being of hundreds of communities and thousands of your constituents depend upon their judgement alone. And, you will have given up perhaps the best opportunity yet to express your frustration and indignation at the insensitivity of our neighbors to the north to the plight of our workers and their families.

At the very least let us send a strong message to the Administration. Let that message be: We have considered your request and must disapprove the "fast-track" procedure until such time as the timber issue is resolved.

Again, I wish to thank my colleagues for providing this opportunity to restate my position on the issue.

Senator **Danforth**. Are there any questions of this panel? Senator Pryor.

Senator **Pryor**. Yes. Thank you, Mr. Chairman. Mr. Nichols, I am sorry I did not get to hear your statement from the furniture industry. Right now, I understand—and you may have covered this in your statement—there is approximately a 3-percent duty on furniture imported from Canada into this country and a 16-percent duty on our furniture shipped to Canada. Now, under a free trade agreement, who do you think would most likely come out ahead, given that environment at this time?

Mr. **Nichols**. Senator Pryor, I think the real issue is that we have that significant barrier for our products. I don't think that it would put Canadian manufacturers at a disadvantage. I think the ultimate benefactor would be our industry. We are competitive in every way with the Canadian manufacturer; and I think the ultimate result would be that consumers in both countries would benefit, and it would be a very positive step.

I would also like to take this opportunity to thank you for being an original sponsor of the Fair Furniture Trade Act. We appreciate that. Thank you.

Senator **Pryor**. Thank you. We are going to have an opportunity to visit with the Ambassador in another round; is this correct, Mr. Chairman?

Senator **Danforth**. Yes.

Senator **Pryor**. Thank you very much.

Senator **Danforth**. My apologies for the fact that your appearance occurred during a rollcall vote on the floor. I wasn't able to hear your testimony, and most of the other members were not; but I assure you it will get very careful attention. Thank you very much.

Ambassador **Yeutter**. Senator Bentsen.

Senator **Bentsen**. Mr. Ambassador, I apologize for the delay in your testimony. You made a comment about torpedoing negotiations.

Let me make it very clear, Mr. Ambassador, that I don't think that is the intent of the majority of this committee at all. We don't want to torpedo this. We are talking about procedures. We are looking at a situation where the chairman of the subcommittee has stated that we have been "stiffed." And we have.

We have been stiffed by this administration on trade bills, and I am fed up with it. I want free trade between Canada and the United States all the way—no subsidies—free trade. I would be delighted if we didn't have a Customs official on either side of that border.

And if we had totally free trade and no subsidies on either side, I think we would both benefit magnificently. We would have some winners and we would have some losers. And I know if you get an agreement with the Canadians, we are not going to get all we want out of it and they are not going to get all they want. There will be compromise. I understand that one.

Mr. Ambassador, if you were in charge of trade, I would be delighted to turn you loose. I would bet my chips on you. I think you are tough, and I think you are smart; but I would also say that same thing about Malcolm Baldrige. The trouble is that you have some fellows that rank you; and they have other responsibilities—foreign affairs, defense—and I think too often the economic interests of our country get subordinated to those other things.

There was a time when we could afford that, but that day is gone. In turn, you have the kind of deficit we are having in trade and the transfer of wealth from our country, a transfer of jobs. The economic interest has to be given a priority. That is what concerns me. I think you have a situation where everybody is in charge of trade and nobody is in charge of trade. I would be delighted if you were.

A group of us on March 10 wrote a letter to the President of the United States in response to the information you gave us on section 305 on telecommunications and the trade policy of Canada. I would like to know if that is going to be rolled into the bilateral trade negotiations with Canada.

Ambassador YEUTTER. The expectation, Senator Bentsen, is that it will be. We can, obviously, proceed bilaterally at an earlier time if that seems desirable. We have had some discussions already with our own domestic industry, and that——

Senator BENTSEN. Let me go on. Someone has got a fast clock on me. I just can't believe that I have taken that long.

I just returned from Mexico, and I had a very interesting meeting with the President of Mexico and with Secretary Silva Herzog, Secretary Hernandez, Secretary Sepulveda, Director General Beteta, and others. One of the things I recalled was that last May Bill Brock and Secretary Hernandez agreed to negotiate a bilateral framework agreement for trade between the United States and Mexico.

I would like answers to the following questions: What is the status of that negotiation? Will you submit that agreement to the Congress for approval? What kind of a cross pollenization do you anticipate between the Canadian negotiations and the Mexican negotiations? For example, would the investment provisions be similar? I would like answers to these questions because I think it is terribly important that, as the Mexican Government works on their accession to GATT, that we do the things on the bilateral framework to try and resolve some of these differences.

I think both sides have some leverage to do some things that in the past, may have been politically difficult to accomplish in Mexico.

Ambassador **Yeutter** Yes; I am well aware of your deep interest in Mexico, Senator Bentsen, and to be specific as to the questions, we have indicated to the Government of Mexico—and Hector Hernandez is my counterpart, the Trade Minister—we intend to pursue the framework arrangement negotiation with them, notwithstanding their desire to accede to the GATT. In other words, we don't consider those to be mutually exclusive at all.

We think that a framework arrangement will be helpful in terms of the bilateral relationship, notwithstanding whatever kind of arrangements we make on GATT accession conditions and obviously on their following the GATT rules once they become a GATT member. So, that exercise will proceed.

It is moving very slowly now because it has been caught up in all of Mexico's other problems, which have had higher priority; the whole matter of simply trying to survive their problems of a debt burden.

Senator **Bentsen**. Let me tell you that the President and Secretary Hernandez are pushing very hard for accession; they are talking about trying to get it this fall.

Ambassador **Yeutter**. In my judgment——

Senator **Bentsen**. That is very ambitious, I think.

Ambassador **Yeutter**. Yes. In my judgment, Senator Bentsen, that is unrealistic. They would like to do it by fall because they know the new round of GATT negotiations is going to begin in September, and they would like to be a full participant in that process; but it seems to me that is an inordinately ambitious undertaking.

Our objectives with Mexico are, of course, much less ambitious than they are here in Canada; but you are right. There is a flow of leverage available to us in that Mexican relationship now, and we are clearly going to use it in terms of the conditions—in relation to the conditions on which Mexico will accede to GATT membership. But in my judgment, that will be a relatively long and difficult negotiating exercise.

Senator **Bentsen**. Mr. Ambassador, I want to talk to you again on this another time.

Ambassador **Yeutter**. OK.

Senator **Danforth**. Senator Symms?

Senator **Symms**. Thank you, Mr. Chairman, and thank you, Mr. Ambassador, for what I am sure has been a difficult morning for you; but you are up to the task, and I can see that you are no worse for wear for it.

I just want to reiterate one point that I made [illegible]ny opening statement. In 1976 when then former Governor Reagan came to Idaho in his quest for the then Republican nomination, which he didn't get that year, he gave a speech and I had the privilege of introducing him.

And he called for a North American economic community, which I thought was a good idea then, and I think is still a good idea now.

I basically favor that. I find myself in agreement with what Senator Bentsen just said to you.

I was hoping we could have the timber and some of these other issues that are causing so much consternation settled prior to the time that the free trade agreement would come up. However, in November of last year you gave me an answer to a question and I want to quote it. It is almost identical to what you told Senator Baucus this morning.

I asked: "When will this timber question be solved?" And you said, and I quote: "A short time frame, Senator Symms. Timber is an issue that we must resolve. I believe we are coming very close to having our position in order and probably initiation of a negotiation with the Canadians."

Now, the negotiations have begun. Is the problem that our house isn't in order, or are the Canadians stonewalling us?

Ambassador **Yeutter**. Well, certainly, it has not been an easy negotiation, Senator Symms. As you know, Ambassador Woods is in Ottawa today working on it. We will have a little better judgment on that situation by the end of the day today; but suffice it to say that there has not been a great deal of flexibility demonstrated thus far on the Canadian side.

Senator **Symms**. If that is the case, in that same hearing, we were having problems—and there has been some work done with the Japanese—over the semiconductor markets. I suggested to you that maybe we should pass legislation which would make reciprocity between, say, beef exports and Japanese semiconductors and tie them together.

You said, and I quote: "In the middle of the negotiation, that would not be a responsible course of action." And I am quoting you now: "If the Japanese were not negotiating with us or discussing these issues in good faith, I would say that might be an appropriate response."

So, I get back to the point. I hope that the Canadians don't walk out on Ambassador Woods today because of this statement of the feeling on this Finance Committee. I think most of the Senators on this committee that will vote in favor of a motion to disapprove in their heart would like to have a free trade zone with Canada. But we simply cannot tolerate it.

You take the sawmill worker that has lost his job in Idaho or the lumberjack in the national forest that is no longer working because of the partial impact of the Canadian timber. That person runs out of patience, and we just simply can't go on. So, if we are getting stonewalled, don't you think we have reached a point where we should make some kind of unilateral action on the part of this administration or this Congress, to solve a few of these issues, to demonstrate that we mean business, so we can get on with negotiations?

Ambassador **Yeutter**. Certainly, we are nearing that point in the negotiating environment, Senator Symms. In other words, we have had several sessions with representatives of the Government of Canada now. They understand our position fully. They have articulated their position fully. There is no need for any educational exercises on either side.

We are nearing the point now of fish-and-cut-bait kind of response; and if we are not able to move the two sides together very soon—and my definition of "very soon" would be a considerably shorter time now obviously than last fall when you first asked me this question—then clearly we are going to have to consider what we might do to respond to this situation——

Senator SYMMS. When you say "very soon," do you mean like within the next 20 days or so?

Ambassador YEUTTER. Yes, sir. That is a good estimate.

Senator SYMMS. Good. I think we do have a fast clock. If my colleague from New York will just let me ask one very brief question? A recent study of CEO's of major American companies shows that only 3 percent of them felt that a Canadian-American free trade zone would significantly benefit the United States. And as I have been saying, if it is fair trade, I think that it could significantly benefit both sides; but if it isn't fair trade, I think that is why we have 97 percent of them saying that it won't happen. Do you agree that that is the problem?

Ambassador YEUTTER. Certainly, we have an obligation as negotiators to bring back an arrangement that would resolve that potential concern totally. We can't have a free and open trade area between the United States and Canada unless it is totally fair. It seems to me, Senator Symms, that is implicit in the definition of a free trade zone or a comprehensive free trade arrangement.

Senator SYMMS. Thank you very much. Senator Moynihan?

Senator MOYNIHAN. I wonder if I could say to my friend from Idaho and to Ambassador Yeutter. Just to make a point, I met last October in Ottawa with Mr. James Kelleher; and he wished to be very explicit and I think it is appropriate that we should be, that Canada was not asking for a free trade zone with the United States. They wanted a new trade agreement that would enlarge our relationship but not abolish the boundaries as free trade implies.

Let me say two or three things here. This has been a disturbing morning and afternoon. I see the Ambassador agreeing. I mean, Canada is the most important other country that there is with respect to the United States. It is our most important political relationship, our most important security relationship, and almost as a reflection of both of those things, our most important trade relationship. I believe we do more trade with the Province of Ontario—I think Ontario from New York—than we do with Japan. And for us just to out of hand reject the President's proposal is a rebuke of the President, in my view, and—although we would never intend it—it would be seen I think in Canada as a rebuke to Prime Minister Mulroney, who is certainly as good a friend as we have in the world and as good a neighbor as we ever hoped to have. We don't take part in their politics, but we can recognize friends when we have them.

And I would like to ask you, sir: What should we do here? I mean, we put in jeopardy the whole North American relationship, and we bring into our discussions, as our chairman has made clear, this committee is angry with the administration and intends accordingly to start a trade war with Canada, or something. That frustration produces such conduct. I mean, this administration's fiscal policies has seen the dollar appreciate to unknown levels, and we find ourselves sitting here saying why have the Canadians manipulated their currency so they have a 70-cent dollar?

Well, there is a 70-cent yen and a 70-cent deutche mark and a 70-cent pound and a 70-cent franc. The Canadians haven't done anything. Now, sir, my question to you is: How are we going to fix this up? I think it is clear that this next week we will vote to reject the President's request for a fast track. Well, the President can resubmit.

There is no point in acting like we are leaving this in suspense, unless the chairman wants to tell me there is suspense. I think next week, sir, we are going to reject this. Would you disagree with my estimate?

Senator DANFORTH. I think it is likely that we will. I think we have said two things: One, that we would like to be doing business with the administration rather than being constantly shoved out into the cold; and, second, with respect to the arrangement with Canada, we would like to assure ourselves that some of the pitfalls we see are taken care of before we are truly at a point of no return, before the negotiations are completed and we are left with a fait accompli.

Senator MOYNIHAN. Those are the reasons. But would the record show that I am a Democrat? [Laughter.]

But I understand.

Ambassador YEUTTER. This morning, Senator Moynihan, I would love to shift you over to the other side of the aisle. [Laughter.]

Senator MOYNIHAN. The frustration with the Japanese and our inability to—Senator Danforth and I have packaged a set of bills; we have 34 cosponsors, and we can't get them to the floor. They are mostly dealing with the problems with Japan and such, and they have nothing to do with Canada.

We don't want this to appear to be a political break with the most important other country in the world to us. Should the Secretary of State get involved here?

Mr. Chairman, I would like to suggest that this is important. No thing is more important. I think we should ask George Shultz to come up and talk to us and have him hear us, privately or otherwise.

Senator DANFORTH. We should have Secretary Shultz and Secretary Wallace come and present the administration's point of view. I can guess what it is.

Senator MOYNIHAN. I think that you have the respect that I know you do for Secretary Shultz, and if he sees the situation at this time, he will want to work at it. We are not going to just let this thing be just a train wreck that we walk away from. We are not going to approve this particular mission. There are obviously levels at which we could approve it. I would like to suggest, with great respect to my friend and chairman, that we ask the Secretary of State to come and talk to us.

Senator DANFORTH. Let's talk to Senator Packwood about this, but I have to say that I don't understand the train wreck idea. We have gotten along for 210 years without a free trade agreement with Canada.

And for the Senate Finance Committee to say that, at this time, we do not want to set in motion this negotiating process, is not saying anything with respect to our relationship with Canada. Obviously, we have a very close and friendly relationship with Canada. It is a very important relationship to the United States, but I don't think that these obvious conclusions mean that the Senate Finance Committee is simply putty in the hands of the administration, to be molded in whatever direction the administration wants.

It seems to me we have a role to play in trade policy. Under the Constitution, Congress has the role to play in trade policy.

Senator Moynihan. I think that is right.

Senator Danforth. And to assert some role for ourselves is not to say anything at all with respect to our friendship with Canada. At some future time, if the administration can deal with us, maybe we will grant fast-track authority. This doesn't lock anything out forever.

Senator Moynihan. I know, but can't we be more—can we press for that, because there are terms under which this committee would want this to go forward? And it is such a great change. I mean, 50 years of simple trade negotiations and so forth is getting a jolt here.

Senator Danforth. How is it getting a jolt? We only have one free trade arrangement with any other country in the world, and that is Israel.

Senator Moynihan. It is not a free trade agreement——

Senator Danforth. All right—a bilateral arrangement of this kind with one country in the world, and that is Israel. We have not had it before with Canada. This is something new and different, and I don't see that it is any jolt to our relations with Canada.

Senator Moynihan. It is not my purpose to argue with the chairman here. I am trying to influence him, and I am glad to hear him saying these things. I don't want to keep others from discussing this, but I do want to leave you with the thought that we shouldn't just leave this to go as it will. We will vote the thing down next week, and then we will go on to other matters.

Can't we continue our negotiations with the administration about the negotiations with Canada?

Senator Danforth. My door has been open for 4 or 5 years.

Senator Moynihan. And no one has come through it is what you are saying?

Senator Danforth. Not many. Senator Pryor.

Ambassador Yeutter. I was just there last week, Senator Danforth.

Senator Danforth. Yes; I know. [Laughter.]

Ambassador Yeutter. Sometimes that is the appropriate answer.

Senator Danforth. It is the only answer you get.

Ambassador Yeutter. Not always.

Senator Danforth. Senator Pryor.

Senator Pryor. Thank you, Mr. Chairman. Mr. Ambassador, our distinguished friend from New York, Senator Moynihan, has just characterized this hearing as disturbing. I would like to characterize this hearing that is taking place this morning as fascinating.

Ambassador Yeutter. That it is, Senator Pryor. [Laughter.]

Senator Pryor. And it is fascinating to the extent that we are having a hearing on this issue at all, because what the administration is asking the 20 members of this committee to do is to totally give up any and all leverage that we have over an issue relative to an unfair trading practice in timber. Mr. Ambassador, you may disagree with that, and you are free to; but I have never seen—I don't think—in my brief 3 years on the committee a more bizarre misreading of the sentiment and the frustration that we all feel with the overall trade policy of the administration.

And to that degree—not only do I say it is fascinating, but I agree with Senator Moynihan—it is disturbing and deeply disturbing to me. One, I think that we need to be told. Is it the position—yes or no—of the administration that there should be no linkage between the timber issue and the free trade request. Now, yes or no, is it the administration's position that we should have no linkage of those two issues?

Ambassador Yeutter. The administration and myself personally have commented on that issue a number of times, Senator Pryor; and the position has always been, for months now, that the two should not be linked in terms of the decisions. That does not suggest that we have any less interest in that timber case.

I must tell you, Senator Pryor, that we have been putting as much time, effort, and energy in terms of representing your constituents in Arkansas in timber as we have in probably any other single issue. And I think we are going to come out with a result very favorable to them, unless it is derailed by what has transpired here this morning; and time will provide the answer to that.

Senator Pryor. In all of the negotiations thus far as it relates to timber, have the Canadians yet even admitted that there is an unfair practice on their part of the so-called timber issue?

Ambassador Yeutter. No; but if I were their negotiators, I wouldn't admit it either.

Senator Pryor. The Ambassador from Canada to this country, I don't think, admits it. I have recently visited with him, as other members of the committee have, and certainly, he did not admit it. And I don't think we can get an admission out of them, and that is very troublesome to this particular Senator.

And Mr. Ambassador, if you were in an elective office—in fact, if you were a member of this committee—and you represented a State where the timber industry was perhaps the largest employer in the State, how would you vote on the issue that we will be confronted with next week, as to whether or not to proceed with this agreement?

Ambassador Yeutter. I would vote to grant fast-track authority because I think this is the most important economic issue we have had between the United States and Canada this century. And how we conduct trade, starting in the year 2000 and on for the next century, probably has a lot more to do with how your children and grandchildren are going to live than anything related on the timber problem, which I happen to think will be solved in a matter of weeks rather than years.

Senator Pryor. Mr. Ambassador, we all love the Canadians. I have loved the Canadians since I was a very young child and used to watch the stories about the Royal Canadian Mounted Police, and they always get their man. And right now, I think that the Canadians are really going to get their treaty, and they are going to get a deal that is much better for them than it is for this country.

And I am very surprised that this request has been made until we get something resolved about the timber issue. And I am very frustrated about it and very, very depressed about it, to be honest with you.

Mr. Chairman, if I might, I have four newspaper articles of recent days from various Canadian newspapers that I think should be submitted for the record at this time. And I ask unanimous consent that they be placed at the appropriate part of our record.

I thank the chairman, and I thank the Ambassador.

[The Canadian newspaper articles follow:]

[illegible] No. 514 876 4492 [illegible] 10.86 14:50 [illegible]

[illegible]

THE GLOBE & MAIL, April 10 1986

Lumber issue won't stall trade talks: PM

By Leslie Shepherd
The Canadian Press

Prime Minister Brian Mulroney Wednesday lightly slapped the wrists of American congressmen who are threatening to scuttle freer trade talks unless a knotty lumber dispute is settled first.

Mulroney, tanned after a Florida vacation, reiterated he wants a "clean launch" to the talks without preconditions such as those proposed by senators from lumber-producing states.

However, his speech to the National Forest Congress broke no new ground and was surprisingly mild given that it was probably his last major opportunity to deliver a strong message before Friday when the U.S. Senate holds hearings on the freer trade proposal and officials from both countries resume lumber negotiations in Ottawa.

Mulroney contended he made a forceful pitch when he was in Washington last month meeting President Ronald Reagan and congressional leaders.

"I refused to accept the proposition advanced by some in the United States that the softwood lumber issue must be resolved in favor of the United States prior to the talks beginning," he said.

"I've stated that Canada was a fair trader in lumber and other commodities."

Meanwhile, International Trade Minister James Kelleher said there may be relief in sight — both for Canadian lumbermen hurt by protectionist measures and for the faltering U.S. lumber industry which initiated them.

"In recent weeks, the price of lumber has risen significantly in the United States and this, combined with the downward trend in mortgage rates, is producing higher profits for American lumber producers," Kelleher said.

This, in turn, could reduce the political pressure on Congress to pass protectionist legislation, he said.

There are about a dozen pieces of legislation now before Congress that would directly or indirectly curtail imports of Canadian softwood lumber worth about $3 billion a year.

The Americans argue that Canadian stumpage fees are so low that they amount to a government subsidy, making it impossible for them to compete fairly.

Kelleher reiterated he expects exploratory talks on a freer trade deal could begin in May or June with the more substantial discussions this fall.

Bill Merkin, the deputy U.S. trade representative, agrees with that timing.

Merkin said he expects the talks to last well into 1987.

Mulroney makes pitch to lumbermen

BY HUGH WINSOR
The Globe and Mail

OTTAWA

It is a long way from being an electrician's helper at the Baie Comeau plant of Quebec North Shore Paper Co. to being the guest of honor at the White House.

So the former electrician's helper, now Prime Minister Brian Mulroney, took the occasion of a speech to the Canadian Forestry Association yesterday to tell the lumbermen what he had done for them when he met President Ronald Reagan in Washington last month.

In addition to moving the problems of acid rain up on the U.S. agenda, he had told President Reagan that the current dispute about Canada's softwood exports to the United States should not be allowed to interfere with negotiations for "freer and fairer trade," he said.

The Reagan Administration has agreed to the concept of a "clean launch" for the talks but some members of Congress from lumber-producing states are trying to link the broader trade discussions to the lumber dispute.

"I refused to accept the proposition advanced by some in the United States that the softwood lumber issue must be resolved in favor of the United States prior to the talks beginning," he said.

The speech to the association might have been an occasion for the Prime Minister to make a major statement on the trade negotiations given that the U.S. Senate begins hearings tomorrow on Mr. Reagan's request to Congress for a mandate to negotiate. But Mr. Mulroney chose instead to make it primarily a domestic speech, stressing the importance of the hewers of wood in Canadian history and his Government's steps to fulfil promises for a full forestry department during the 1984 election campaign.

Quoting historian Donald Creighton's description of Ottawa 80 years ago, where politicians had to pick their way around piles of sawdust and sawn lumber to get to Parliament Hill, Mr. Mulroney said there are major changes. "Now you have to fight your way through lobbyists."

The Prime Minister also attempted to differentiate between what he called "question period issues" and real issues such as forestry issues and he assured his audience that he knew the difference.

Speaking of the damage caused by acid rain, Mr. Mulroney said environmental concerns can no longer be separated from economic

No concessions in lumber fight before trade talks, PM declares

By Martin Cohn Toronto Star

OTTAWA — The federal government will not bow to American demands for concessions on Canadian lumber exports before free trade talks begin, Prime Minister Brian Mulroney says.

Despite pressure from some U.S. politicians, Mulroney insisted yesterday that he rejects any links between the lumber dispute and free trade talks, and noted that he said so to President Ronald Reagan in Washington last month.

"I impressed on President Reagan and congressional leaders the importance of a clean-launch concept to any trade negotiations," Mulroney told a forestry convention.

"I refused to accept the proposition advanced by some in the U.S. that the softwood lumber issue must be resolved in favor of the U.S. prior to the talks beginning."

Free trade talks, which would remove most trade barriers between the two countries, are expected to begin next month, if Congress gives its go-ahead later this month.

Meanwhile, the fourth round of bilateral talks on the lumber dispute will take place in Ottawa tomorrow.

Mulroney

Some congressmen from the U.S. West have accused Canada of unfairly subsidizing lumber exports because companies pay low stumpage fees on crown-owned lands. The congressmen want a settlement of the dispute before free trade talks begin.

Mulroney noted that Ottawa's free trade drive is the most important government initiative concerning the forestry sector.

Canada's $15 billion in forestry exports need clear access to U.S. markets through free trade, to head off of rising protectionism in that country, he said. About 70 per cent of Canada's forestry exports now go to the United States.

"We are looking first to our closest ally and neighbor to secure our markets," the Prime Minister said.

Trade Minister James Kelleher also warned the forestry delegates that "the spectre of protectionism is rising again, particularly in our largest market, the United States."

Ottawa is monitoring the progress in Congress of protectionist bills, which would increase barriers to Canadian experts. "We are fighting these forest fires with every tool at our command," Kelleher said.

He cited a ruling by the U.S. commerce department that Canadian timber is not unfairly subsidized, and added that Ottawa enjoys White House support on the issue.

William Merkin, the Americans' deputy trade representative, told the delegates that the Reagan administration is strongly resisting congressional efforts to link free trade talks to the lumber issue.

Indeed, Merkin said American forestry producers also benefit from various forms of government aid. "Our hands are not necessarily clean — I'm not sure how dirty."

Canadian forest industry facing crisis, say experts

By April Lindgren
Citizen staff writer

Outdated equipment, failure to adequately replenish timber supplies and overly optimistic estimates of Canada's forest resources have thrown the industry into a state of crisis, industry experts said Wednesday.

The 450 business, academic and government representatives attending the National Forest Congress spent the first day listening to a discouraging outlook for an industry which employs one out of every 10 Canadians and contributes nearly $30 billion to the economy annually.

Indicators of the crisis presented by speakers touched on everything from trade issues to timber shortages:

- Abitibi-Price president R.K. [illegible] described a "dwindling" [illegible] in Canada's world market [illegible] world paper and paperboard market declined to 7.7 per cent in 1983 from 9.8 per cent in 1965, "more deterioration than any other producing country."

In newsprint, the country's traditional stronghold, market share has declined from 41 per cent to approximately 33 per cent in the same period.

- A study of international newsprint competitiveness involving six major newsprint producers ranked Canada lowest in cost competitiveness, reflecting the lower productivity of older machinery and slower adaptation to new technology.

- University of British Columbia forestry professor Les Reed said that past estimates of Canada's timber supply have been much too optimistic and that shortages [illegible] already are being experienced by [illegible] mill operations in British [illegible]

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B

Plans change:
Coates not going
to South Korea
Page B-5

The Gazette
CANADA
• MONTREAL, THURSDAY, APRIL 10, 1986

Hôtel du Parc
BANQUETS
Meet with us first.

We'll give PCs bloody fight over free trade: CLC

By TERRANCE WILLS
Gazette Ottawa Bureau

OTTAWA — The Progressive Conservative government will have a bloody fight on its hands from organized labor in trying to reach a free-trade deal with the United States, a labor leader warned yesterday.

James Buchanan, president of the Canadian Paperworkers Union and a vice-president of the Canadian Labor Congress (CLC), told a national forest conference:

"The government has not been given a mandate from the people of Canada to put in jeopardy our cultural and social way of life. The blood will be on their hands, and there will be blood the way they are going."

The CLC and other opponents of a free-trade deal plan a mass demonstration on Parliament Hill a week from today.

Trade Minister James Kelleher was on stage a few feet from Buchanan as the labor leader issued the warning, while Prime Minister Brian Mulroney had just left.

In his remarks, the PM made clear that a trade deal with the U.S. remains one of his government's highest priorities.

"In a world of increasing trade disruptions and protectionism, we are looking first to our closest ally and neighbor to secure our markets and explore new opportunities," Mulroney said.

The top U.S. trade official on Canadian issues, who also addressed the conference, replied that the U.S. administration is just as keen to reach a bilateral trade deal as the Mulroney government.

Bill Merkin, deputy assistant U.S. trade representative, told the conference organized by the Canadian Forestry Association:

"We are firmly committed to these negotiations and applaud the prime minister for this proposal.

"I believe we have a historic opportunity here, an almost once-in-a-lifetime opportunity, to try to construct a trading relationship between the two largest trading countries in the world that will benefit generations to come in both countries and be an example to the rest of the world."

Merkin predicted that Congress will give approval this month for a "clean launch" of the talks, meaning Canada will not have to rein in its softwood lumber exports to the U.S. as a precondition. Several U.S. senators have complained that Canada has grabbed too big a share of the U.S. market — about a third — forcing many U.S. mills to close.

Both Merkin and Kelleher predicted that preliminary negotiations for a free-trade deal could start as early as next month, while the hard bargaining will begin in the fall.

Merkin said that, by the end of next year, the administration intends to assess whether the negotiations have reached a stage that a deal can be made.

President Ronald Reagan told Mulroney in Washington last month that he wanted to see a trade agreement in place before he leaves the White House. The next presidential election is in November 1988.

"The next year and a half will be a very intensive period (of negotiation)," Merkin said. "I am confident. Maybe in two years we can get back up and report success."

Both Merkin and Kelleher said the deal would have to be phased in slowly to allow industries facing new competition to adapt.

Subsidies to industry on both sides of the border will be a big issue in the negotiations, Merkin said.

"Our hands are not necessarily clean," Merkin conceded when asked from the floor whether state and local governments in the U.S. do not provide just as many subsidies to industry as are made in Canada through regional development grants.

BEST COPY

Merkin predicted that Congress will give approval this month for a "clean launch" of talks, meaning Canada will not have to rein in its softwood lumber exports to the U.S. as a precondition. Several U.S. senators have complained that Canada has grabbed too big a share of the U.S. market -- about a third -- forcing many U.S. mills to close.

Senator DANFORTH. Senator Baucus.

Senator BAUCUS. Thank you, Mr. Chairman. Mr. Ambassador, a few minutes ago Senator Moynihan from New York made a statement that I think is a very important statement. After all, he was Ambassador from our country to India and he has been in the U.N. He has very appropriately commented on U.S. foreign policy and U.S. international relations.

He said that this development this morning is very disturbing. He also went on to suggest that perhaps we are in a trade war with Canada. Now, frankly, I think that, as much as I respect his position, he is speaking of a situation that is not fully on target with what is happening here today.

I would not characterize this development as disturbing. I would characterize it as sobering, as realistic; in fact, I think it will help strengthen our relationship with Canada. Canada has always been a very close friend of the United States; very close. I cannot think of a closer friend that has endured through the times of strain and the turmoils of international developments over the years than Canada.

But I also think that whenever there are two neighbors, there are two individuals, that that relationship is strengthened when there is more honest, candid dialog between the two. It is clear that we are both trying to accomplish the same objectives—to increase our economic growth, to increase it through freer trade, to try to reduce the impediments to trade, whether they be tariffs, nontariff barriers—whatever they may be. That is the goal we are all striving for, but I think that at this point it is important for us to be more honest with our Canadian friends to the north, more honest in saying that we see some problems. You cannot take advantage of us. You cannot try to help yourself at our expense because we, on our side of the border, see these problems.

And I think that these problems have to be ironed out; they have to be resolved more to the satisfaction of Congress than has been the case thus far so that we can proceed and work toward a free trade agreement.

If I might add, Mr. Ambassador, I think that it will strengthen your hand as negotiator if we do vote a motion of disapproval without prejudice, or at least make it clear to Canada and to the administration that our goal is still the same: a free trade agreement. Because if we disapprove at this time, you then will be able to sit down at the bargaining table with more authority, more leverage, more bargaining power, and say to Canada that certain agreements have to be reached before you can come back to the Congress for a straight up or down vote, to ratify or not ratify, a free trade agreement.

So, I think this hearing this morning has been very helpful; it has been very constructive. It has been very good, very beneficial; and I think it has been so because it has been honest, it has been direct, and it has therefore, I think, helped strengthen our relationships. So, it is my hope that next week will be merely a formality in the process. Next week when we vote to disapprove, it will be just one of many processes as we go down the road to get a stronger bilateral economic relationship with our good friends to the north.

Ambassador Yeutter. I hope you are right, Senator Baucus. I really do because, as Senator Moynihan indicated, it is a tremendously important binational relationship. I do believe, using Senator Danforth's terms, that it will be read as a huge jolt in Ottawa today; and I am fearful it will be read in destructive rather than constructive terms, but time will tell.

We will know within the next 24 hours or so what the reaction in Ottawa would be. But I can tell you, Senator Baucus, and I truly believe you are sincere in your comments, we really do not want this to impede the development of a friendly relationship. You are representing a State that is right on the border and has a lot at stake here.

I am very worried about the response because I think there is a chance that it could jeopardize relationships in an unhealthy way.

Senator Baucus. I understand that, but I think it is part of human nature to have an overreactive initial response. I think the Canadians' initial reaction will be very strong, very severe; but I think that as Canada begins to reflect on the development—more calmly reflect on it—I think they will realize that maybe there is a lot to be gained here. Maybe this is a blessing in disguise to help to improve our countries' ties.

Senator Danforth. Mr. Ambassador, thank you very much. You have been very patient.

Ambassador Yeutter. Thank you.

[Whereupon, at 12:54 p.m., the hearing was adjourned.]

[The following material was submitted for the record:]

TESTIMONY OF
SENATOR DALE BUMPERS
BEFORE THE SENATE FINANCE COMMITTEE
APRIL 11, 1986

Mr. Chairman, I very much appreciate your permitting me to testify before the Finance Committee on the question of the proposed negotiations about a U.S.-Canada free trade zone. These negotiations potentially have a significant impact on the state of Arkansas, which I would like here to discuss.

Let me be clear about my position; the United States should not begin negotiations about a free trade zone with Canada until Canada ceases providing an unfair subsidy for its timber producers. The only way in which the U.S. can make progress on the timber subsidy issue is hold off negotiations on the free trade zone until the subsidies are eliminated.

If the Finance Committee gives the President the green light to begin netotiations with Canada, Canada will have every incentive to postpone resolution of the subsidy issue until the very end of these negotiations, when the really hard bargaining will begin and when the Canadian subsidy practice will be valuable to Canada as a bargining chip.

I have heard estimates that these negotiations may take three to five years to complete. If Canada can continue to avoid the timber subsidy issue throughout these negotiations, Canada may even drag out these negotiations longer than that. While there's talk, there will be no action.

The Committee also should reject the President's request until he and his deputies show some understanding of the timber subsidy issue. Only then will I have some confidence that the interests of U.S. timber producers will be protected in these negotiations.

The current attitude of this Administration on timber imports could not be less encouraging. Commerce Secretary Baldridge appeared before the Appropriations Committee a few weeks ago and I asked him whether the Department has reconsidered its position in the Softwood Lumber case in light of the decision of the U.S. Court of International Trade in the Carbon Black case, which held that the Department's legal rationale in both cases was non-sensical. He said the Department had not changed its position.

I then asked Secretary Baldridge how U.S. negotiators could have any credibility in arguing that the Canadian stumpage system constitutes a subsidy when the U.S. government has explicitely rejected that finding and continues to reject this finding. He had no answer to this question.

As if this weren't bad enough, the President has explicitely stated that he will veto any meaningful trade bill adopted by Congress, particularly any bill which contains any provision on the natural resource subsidy issue. In 1984 the President made this threat and, as a direct result, the natural resource subsidy provision in the Trade Remedies Reform legislation was deleted.

If our government agrees with Canada on the subsidy issue and if the President will prevent the Congress from taking any action against Canadian subsidies, why does Canada have any incentive to negotiate? Then, if the U.S. permits Canada to fold the natural resource subsidy issue into the larger free trade negotiations, Canada can ignore any protests it hears from U.S. timber producers at least until the final bargaining sessions three or four years from now. By then U.S. timber producers will be so weak, they may not be able to mount an effective protest.

I am aware that there have been some meetings between U.S. and Canadian representatives on the timber subsidy issues, but it should come as no surprise that Canada would be willing to talk, especially now when Congress still could reject the negotiations on the free trade zone. A little talk now by Canada can prevent actions for years to come. The Administration can huff-and-puff about the timber subsidy issue, but when it comes right down to it Canada knows that this Administration agrees with Canada on this issue.

Failing to reject the President's request for negotiating authority effectively endorses his and Canada's do-nothing approach to the timber subsidy issue. Until we get the President's attention on this issue and until he and his advisors come to see the Canadian stumpage system as a subsidy, I am hesitant about the President negotiating with Canada and, in any event, Canada will not listen if he does raise the issue. As it stands now our President does not represent the interests of U.S. timber producers. Until we get his attention he will continue to agree with Canada and protect its interests from any action by Congress.

I urge the Committee to reject the President's request and put both our President and the Canadian government on notice that this timber subsidy issue must be resolved now and it must be resolved first.

Bumpers

ADDITIONAL STATEMENTS

[illegible]

TIMBER COMES FIRST IN CANADIAN NEGOTIATIONS

● **Mr. BUMPERS.** Mr. President, on Friday, the Finance Committee will hold an important hearing on the question of the proposed negotiations about a United States-Canada free trade zone. These negotiations potentially have a significant impact on the State of Arkansas so I have submitted a written statement to the Finance Committee making a series of points.

Let me be clear about my position: The United States should not begin negotiations about a free trade zone with Canada until Canada ceases providing an unfair subsidy for its timber producers. The only way in which the United States can make progress on the timber subsidy issue is hold off negotiations on the free trade zone until the subsidies are eliminated.

If the Finance Committee gives the President the green light to begin negotiations with Canada, Canada will have every incentive to postpone resolution of the subsidy issue until the very end of these negotiations, when the really hard bargaining will begin and when the Canadian subsidy practice will be valuable to Canada as a bargaining chip.

I have heard estimates that these negotiations may take 3 to 5 years to complete. If Canada can continue to avoid the timber subsidy issue throughout these negotiations, Canada may even drag out these negotiations longer than that. While there is talk, there will be no action.

The committee also should reject the President's request until he and his deputies show some understanding of the timber subsidy issue. Only then will I have some confidence that the interests of U.S. timber producers will be protected in these negotiations.

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Failing to reject the President's request for negotiating authority effectively endorses his and Canada's do-nothing approach to the timber subsidy issue. Until we get the President's attention on this issue and until he and his advisers come to see the Canadian stumpage system as a subsidy, I am hesitant about the President negotiating with Canada and, in any event, Canada will not listen if he does raise the issue. As it stands now our President does not represent the interests of U.S. timber producers. Until we get his attention he will continue to agree with Canada and protect its interests from any action by Congress.

I urge the Finance Committee to reject the President's request and put both our President and the Canadian Government on notice that this timber subsidy issue must be resolved now and it must be resolved first ●

Buffalo Area Chamber of Commerce

TO: Senator Bob Packwood, Chairman and Members
of the Senate Finance Committee

RE: Bilateral Trade Negotiations with Canada

The Buffalo, New York Area Chamber of Commerce views with a great deal of concern the opinions voiced at the Senate Finance hearing in opposition to the commencement of bilateral trade negotiations with Canada. In our opinion, such action would not be in the best interests of the United States or the industries most critically involved.

There is a great need for freer trade between our two countries and these negotiations, if properly conducted, should have that result. All subjects of concern should be on the table for discussion, such as our "lumber" and "cultural" problems with Canada and their "quota" problems with us. If the negotiations are approached freely and openly, there is at least a reasonable possibility of achieving some progress on those problems which presently appear to be of primary concern to those Senators expressing a negative opinion.

Furthermore, there is a great likelihood of progress in other less controversial areas. The opportunity for substantially increased exports with resulting economic benefits to the United Sates becomes a very real possibility. A simple example demonstrates this. The United States presently provides

72% of Canada's imports. However, there is still a trade imbalance with Canada of 11 billion dollars. Canada imports 21 billion dollars from other countries. With preferred access to the Canadian market, a larger share can go to the United States.

Furthermore, and perhaps more important is the fact that freer trade can result in an expansion of the Canadian market to export from the United States. This is evident from the success of the Autopact. Auto related imports now amount to 31% of the Canadian total imports from the United States. No other imports from the United States even remotely approach this percentage. There is no reason to believe that freer access to the Canadian market would not have, if not equal, at least improved results for many manufacturing and service industries.

As we are all aware, both Canada and the United States face ever increasing competition from the Far East, particularly Japan and Korea, and from other trading nations. A free trade agreement with Canada can create a much stronger economic unit to better meet this competition.

Canada is the United States' largest trading partner. We export twice as much to Canada as we do to Japan. Approximately two million American jobs are dependent on exports to Canada and many of those are in border states which can ill afford further job erosion. One cannot be certain that the status quo will be maintained by Canada in the face of a rejection of this magnitude. It must be remembered that this is the first time Canada has ever approached the United States for this purpose. (Indeed the "status quo" is rarely maintained in any event.) Not to enter into negotiations with a neighboring country which has consistently been our best friend (as has just been most graphically illustrated) sends a message to that country and to the rest of the world which is at best counter-productive and possibly worse.

These will be difficult negotiations. Canada has far more reason to be concerned about the results of these negotiations than we, simply because of our relative sizes. Let us at least match Canada's courage by going forward.

Respectfully yours,

Eric Swider
President

Attachment

EXAMINATION OF THE ECONOMIC RELATIONSHIP BETWEEN CANNADA AND THE UNITED STATES TO SUPPORT THE CREATION OF A BILATERAL FREE TRADE AGREEMENT*

I. OVERVIEW:

The global trading environment is being reshaped by major forces of economic change. Many of these emanate from the developing countries, particularly because of the rapid growth of their industrial capacity. A number of so-called "newly industrialized countries" (NIC's), including South Korea, Brazil, and Mexico, as well as such Mediterranean countries of Spain and Greece, are developing heavy industries. These manufacture capital goods such as steel and transportation equipment that were formerly produced mainly by the advanced industrial countries in Europe and North America.

The NIC's (Table 1) have now reached levels of production sufficient to reap major economies of scale and, hence, are able to compete with basic heavy industries in the industrial countries. Furthermore, a host of lower-wage developing countries, including China, Thailand, Malaysia, the Philippines and India, are expanding production in textiles, footwear, clothing, and labor-intensive, light manufacturing of consumer electronics. In the long term, this is often unbeatable competition for similar industries located in countries such as United and States and Canada that have relatively high labor costs(21, p. 3).

With these rapid developments in technologies and permanent shifts in competitiveness, North America is going through some wrenching economic changes. All of these are changing the economic landscape, creating new businesses, destroying or remodelling old ones, and leaving in their wake serious problems of unemployment and long-term competitiveness. Through the smoke and dust, we have started to perceive that adjustment to these forces will encourage Canada and the United States to come yet closer together.

*Mary Elizabeth Mokka

TABLE I

Industrial and Economic Indicators, Selected Countries 1970 - 1982

(average annual percentage change)

	GNP PER CAPITA*	CONSUMER PRICES	GROSS DOMESTIC INVESTMENT	EXPORTS	MANUFACTURED OUTPUT
CANADA	3.1	9.3	3.3	4.0	2.5
UNITED STATES	2.2	7.3	1.3	5.6	2.4
JAPAN	6.1	6.9	3.3	8.5	6.6
ARGENTINA	1.6	136.0	1.0	8.3	-0.2
BRAZIL	4.8	42.1	6.5	8.8	7.8
SOUTH KOREA	6.6	19.3	11.0	20.2	14.5

* Growth of GNP per capita is for the period 1960 - 1982

Source: World Development Report 1984 (New York Oxford University Press for the World Bank, 1984)

Economic forces have long made us good, close neighbors, and these ties have been strengthened by having one language in common and largely similar cultural and political values. The U.S. and Canada are each other's largest trading partner. Canadians seldom forget this: the U.S. accounts for about 70 percent of Canada's total trade. Amid their trade battles with Europe, Japan, and some industrializing countries, it is easy for Americans to overlook the relatively peaceful flows across their northern flank, which take up about 20 percent of their total trade.

I. OVERVIEW:(CONT.)

The U.S. consistently enjoys a significant surplus of trade with Canada in services and manufactured end products. In contrast, Canada has traditionally had a surplus of trade in resource-based goods: wood and paper products, petroleum and natural gas, electricity, and metals.

Canada and United States are - and will remain in the foreseeable future - each other's most important partner. Two-way trade is approaching $125 billion annually, and cross-border investments are near the $70 billion mark. The United States does more trade with the province of Ontario than it does with Japan, and more trade with the province of British Columbia than with all of China. The United States has more capital invested in Canada than in any other country, and Canadian investments in the U.S. exceed the total of its investments in the rest of the world (20, p. 20).

II. ECONOMIC TRENDS IN CANADA/UNITED STATES:

Canada and the United States have the largest bilateral trade and economic relationship in the world. In 1984, two-way trade exceeded U.S. $112. billion.

In 1984, U.S. exports to Canada grew by almost 27 percent, as opposed to the average growth of 8.7 percent for other export markets. U.S. exports to Japan grew by 7.6 percent in 1984, while exports to the EEC grew by 6 percent.

II. ECONOMIC TRENDS IN CANADA/UNITED STATES: (CONT.)

The United States exports twice as much to Canada as it does to Japan. Further, these U.S. exports are equal to those of all the countries of European Economic Community. Approximately 85 percent of these U.S. exports to Canada, in 1984, were manufactured and semi-finished goods; comparable figures for Japan and the EEC were 25 percent and 64 percent respectively. Currently, about 2 million American jobs depend directly on U.S. exports to Canada (6, p. 3).

In 1984, the United States supplied Canada with U.S. $52.9 billion or 72 percent of the total Canadian imports of U.S. $73.9 billion. During this same period the United States took U.S. $63.9 billion, or 73 percent of total Canadian exports of U.S $4.6 billion.

The United States has approximately U.S. $90 billion in direct and indirect investment in Canada, representing more than 75 percent of all foreign direct investment in Canada. Canada has U.S. $30 billion in direct and indirect investment in the U.S. making Canada the third largest source of investment funds for the United States (Ibid.).

II. ECONOMIC TRENDS IN CANADA/UNITED STATES(CONT.)

CANADA/U.S. ECONOMIC INDICATORS

I. CANADIAN TRADE

	WITH ALL COUNTRIES		WITH THE U.S.A.	
	EXPORTS	IMPORTS	EXPORTS	IMPORTS
	($ billion CDN.)		($ billion CDN.)	
1980	76.2	69.3	48.2	48.5
1981	83.8	79.5	55.5	54.5
1982	84.5	67.9	57.7	47.9
1983	90.9	75.6	66.3	54.1
1984	112.5	95.8	85.1	68.5

II. PERCENTAGE CHANGE

	WITH ALL COUNTRIES		WITH THE U.S.A.	
	EXPORTS	IMPORTS	EXPORTS	IMPORTS
1980	16.0	10.2	8.2	6.7
1981	10.0	14.7	15.2	12.2
1982	0.9	-14.6	4.0	-12.2
1983	7.6	11.4	15.0	13.0
1984	23.8	26.7	28.4	26.6

II. ECONOMIC TRENDS IN CANADA/UNITED STATES:(CONT.)

CANADA/U.S. ECONOMIC INDICATORS

III. PERCENTAGE DISTRIBUTION OF EXPORTS AND IMPORTS IN 1984

Exports from Canada

To: United States	75.6%
Japan	5.1%
European Community	6.3%

Imports by Canada

From United States	71.5%
Japan	5.9%
European Community	8.6%

IV. LEADING CANADIAN EXPORTS TO THE USA IN 1984 IN MILLIONS OF CDN. DOLLARS

1.	Passenger autos and chassis	13,670.00
2.	Motor vehicle parts (except engines)	7,400.00
3.	Trucks, truck tractors and chassis	5,316.00
4.	Crude petroleum	4,374.00
5.	Newsprint paper	4,056.00
6.	Natural gas	3,886.00
7.	Lumber, softwood	3,271.00
8.	Petroleum and coal products	3,023.00
9.	Motor vehicle engines and parts	2,085.00
10.	Wood pulp and similar pulp	2,062.00

II. ECONOMIC TRENDS IN CANADA/UNITED STATES:(CONT.)

CANADA/U.S. ECONOMIC INDICATORS

V. LEADING CANADIAN IMPORTS FROM THE USA IN 1984 IN MILLIONS OF CDN. DOLLARS

1.	Motor vehicle parts(except engines)	12,477.00
2.	Passenger automobiles and chassis	6,085.00
3.	Electronic computers	3,888.00
4.	Trucks, truck tractors and chassis	1,829.00
5.	Motor vehicle engines	1,281.00
6.	Electronic tubes and semi-conductors	1,259.00
7.	Coal	1,093.00
8.	Precious metals including alloys	1,016.00
9.	Other telecommunications equipment	1,004.00
10.	Other chemical products	959.00

Source: Statistics Canada

VI. FOREIGN INVESTMENT

	($ Billion CDN)
U.S. Direct Investment in Canada	64
U.S. Portfolio Investment in Canada	58
Canadian Direct Investment in the U.S.	30
Canadian Portfolio Investment in the U.S.	11

Source: Statistics Canada 1984 cumulative estimates in Canadian dollars)

III. ANALYSIS:

A) THE CANADA/U.S. BORDER - HOW OPEN IS IT?

Since the mid-1950's, Canada's import policy has been moving slowly toward freer trade and dismantling the highly protectionist National Policy of 1879. However, Canada's average tariff rate will still be 9.2 percent after January 1, 1987, the day the last phase of Tokyo round tariff cuts (General Agreement on Trade & Tariffs) come into effect worldwide. By contrast, the average U.S. tariff will be 4 - 5 percent, and 6 - 7 percent in the EC and Japan. "Commentators like to remind us that by 1987, 85 percent of all Canada-U.S. trade will be tariff-free," says one senior trade official (13, p. 8). "That doesn't take into account the trade that simply doesn't take place because of high tariff protection above 15 percent, and even 20 percent in some product areas" (Ibid.).

In 1987, the Canadian tariff will range from more than 9 percent for many manufactured goods (automobiles imported from outside North America, for example, will carry a duty of 9.2 percent) to more than 15 percent for ships, pleasure crafts, railway cars, textiles, clothing, footwear, carpeting, tools, clocks, and telephones. Exceptions falling outside the range include color televisions (7.5 percent), computers (3.9 percent) cement products (8 percent), cameras (7.5 percent), and office equipment, aircraft, radios, stereos, and fertilizers (tariff-free).

ANALYSIS (CONT.):

A) THE CANADA/U.S. BORDER - HOW OPEN IS IT?(CONT.)

The Canadian producers are also concerned about their access to the U.S. market. More than two million workers depend on this access. In addition to problems arising from a lack of predictability, there is a number of specific barriers that many think should be reduced. These include:

- The manner in which Canadian companies' access to the U.S. market can be frustrated by the use of trade remedy laws.
- The ease with which imports from Canada are swept up in measures aimed at third world countries.
- The continual threat of unilateral changes in the rules of the game.
- The lack of access to the U.S. procurement market due to "Buy America" provisions at the federal and state levels.
- The large number of U.S. tariffs which continue to limit access to that market.
- The inadequacy of current mechanisms to resolve disputes.

High tariff and other restrictions provide substantial protection to producers of books, benzenoid chemicals, ceramic tiles, canned tuna, rubber footwear, steel, textiles, motorcycles, peanuts, dairy products, and more. Indeed, significant trade barriers cover more than a quarter of all manufactured goods sold in the U.S., and cost American consumers more than $50 billion a year, or $450. for every working man and woman, according to Gary Hufbauer, a Georgetown University Professor, in a book to published later this year (23, pp. 1, 14).

ANALYSIS (CONT.):

A) THE CANADA/U.S. BORDER - HOW OPEN IS IT?(CONT.)

The U.S. and Canada have been caught up in the global trend toward a "new protectionism," establishing quotas, "voluntary" import restrictions, and other barriers rather than tariffs to shield its domestic industries from foreign competition. By Mr. Hufbauer's estimate, the percentage of U.S. imports covered by protection has risen to 21 percent today from 8 percent in 1975 (Ibid.). America's trade barriers impose large costs on U.S. consumers. And while they may save jobs in protected industries, economists say barriers reduce jobs elsewhere in the economy. According to a recent study by the Federal Reserve Bank of New York, it is estimated that consumers pay a tax of as much as $12 billion a year to protect the U.S. textile industry (23, p. 14).

B). EVIDENCE OF INCREASING INTERDEPENDENCE

Trade, in a broad sense, includes the two-way movement of people, goods, services, investment money, and information, and properly tended, it is broadly enriching. In spite of the trade barriers mentioned previously, Canada and the United States exchanged U.S. $118 billion worth of goods last year. The United States sells more to the province of Ontario than it does to Japan or to all of Western Europe; and Canada sells more to the United States than it does to the rest of the world. In 1984, the growth of Canada's exports to the U.S. was more than its total exports to Europe and Japan.

Since the end of World War II, the distinct long-term trend has been that the U.S.A. has been taking a larger and larger share of Canadian exports - from around 50 percent in the late 1940's to more than 70 percent now (Chart VII).

ANALYSIS (CONT.):

B) EVIDENCE OF INCREASING INTERDEPENDENCE (CONT.)

During 1983, the U.S. market absorbed 72.9 percent of Canada's exports to the world. The figure for 1984 is even higher. Canada's next largest export market was Japan at 5.2 percent (Chart VIII). This highlights the importance of secure access to the U.S market as an essential condition for Canada's well-being.

The economic pull in Canada's region has always been to the south, toward its North American neighbor with somewhat similar geography, agriculture, and industry. As a result, Canadians have clustered along the southern border. In fact, almost all Canadians live within 200 miles of the border, and the majority lives within 50 miles.

The American industrial and business presence, too, is very tangible. Companies based in the U.S. or consortiums own much of the refining and marketing of Canada's oil, its chemical industry, its production of electricity, goods, and heavy machinery. Canada's major automobile industry is about 90 percent American owned (10, p. 54).

All this helps account for why the U.S. has loomed so large in the Canadian consciousness, while Canada has occupied a substantially dimmer image in the American mind. However, unbeknown to most Americans, Canada has a major impact on their economy and daily lives. The Canadian presence in the U.S. covers the gamut from banking to utilities, farming, real estate, manufacturing, entertainment, and communications. Many of the books, newspapers, and magazines Americans read were printed on Canadian paper; much of the electric power they

ANALYSIS (CONT.):

B) EVIDENCE OF INCREASING INTERDEPENDENCE(CONT.)

consume on the East Coast and in the Midwest comes from Quebec, Ontario or Manitoba; in New York City, the giant Battery Park complex is being built by Toronto's Olympia & York, one of Manhatten's biggest landlords; and the subway cars New York City tenants will take to Battery Park could well have been built by Montreal's Bombardier. The list is endless - from Molson's beer, to Harlequin novels, to Savin copiers, to DeHavilland airplanes (recently bought out by Boeing Corp. in the U.S.), to the arms that lift payloads from the base of a U.S. space shuttle - they were all made in Canada.

In similar fashion, an estimated two million Americans are employed directly or indirectly in the export trade to Canada. Slightly more than half of the exports are produced by workers in twelve states. Eight of them - Michigan, Ohio, Pennsylvania, Wisconsin, New York, Washington, Illinois and Indiana - are on the border, and the others - California, New Jersey, Texas and Massachusetts - are major industrial centres. Most of the trade going north is in manufactured goods (5, p.7).

C). ADVANTAGES FOR CANADA

There are several advantages for Canada:

1) A free trade area with the U.S. would increase the liberalization of trade instead of the inward-looking option of raising new barriers to trade.

ANALYSIS (CONT.):

C) **ADVANTAGES FOR CANADA (CONT.)**

2) It would remove the remaining tariffs on Canadian-U.S. trade. Although the Tokyo Round has reduced tariffs substantially, remaining U.S. tariffs still exert a substantial restraining effect on Canadian exports to that country. Table III lists the average tariff rates for major industrial sectors in Canada and the U.S. Tariffs are particularly high on petrochemicals, textiles, fashion goods, clothing, and some types of electronic and telecommunication equipment.

3) It would also reduce nontariff barriers and clarify their applicability.

4) It would provide Canadian firms with secure access to a market of over 250 million people. This would allow them to achieve competitive costs based on large economies of scale and long production runs.

5) These low costs would make it easier to export to third countries and poised to compete in the expanding markets of the newly industrializing countries.

TABLE III

POST TOKYO ROUND TARIFFS IN INDUSTRIAL PRODUCTS BY SECTOR: CANADA, UNITED STATES AND ALL INDUSTRIAL COUNTRIES

(percentage)*

SECTOR	CANADA	UNITED STATES	ALL INDUSTRIAL COUNTRIES
TEXTILES	16.7	9.2	8.5
WEARING APPAREL	24.2	22.7	17.5
LEATHER PRODUCTS	6.3	4.2	3.0
FOOTWEAR	21.9	8.8	12.1
WOOD PRODUCTS	3.2	1.7	1.9
FURNITURE AND FIXTURES	14.3	4.1	7.3
PAPER AND PAPER PRODUCTS	6.7	0.2	4.2
PRINTING AND PUBLISHING	1.0	0.7	1.5
CHEMICALS	7.5	2.4	6.7
RUBBER PRODUCTS	6.7	2.5	4.1
NONMETAL MINERAL PRODUCTS	6.4	5.3	4.0
GLASS AND GLASS PRODUCTS	7.2	6.2	7.9
IRON AND STEEL	5.4	3.6	4.4
NONFERROUS METALS	2.0	0.7	1.6
METAL PRODUCTS	8.5	4.8	6.3
NONELECTRICAL MACHINERY	4.5	3.3	4.7
ELECTRICAL MACHINERY	5.8	4.4	7.1
TRANSPORTATION EQUIPMENT	1.6	2.5	6.0
MISCELLANIOUS MANUFACTURES	5.4	4.2	4.7
ALL INDUSTRIES	5.2	4.3	5.8

* WEIGHTED BY OWN-COUNTRY IMPORTS, EXCLUDING PETROLEUM

SOURCE: A.V. Dearcorff and R.M. Stern, "Economic Effects of Complete Elimination of Post-Tokyo Round Tariffs," in W.R. Cline, Trade Policy in the 1980's (Washington, D.C.; Institute for International Economics, 1983) pp. 674-675.

ANALYSIS:

D) ADVANTAGES FOR THE UNITED STATES

The economic significance of Canada to the United States of often underestimated. As of 1983, U.S. direct investment in Canada had a book value of U.S. $47.5 billion, accounting for about 30 percent of U.S. direct investment in the industrial countries (Chart IX). In 1983, U.S. exports to Canada amounted U.S. $43.8 billion or 22 percent of U.S. exports (Chart X). In comparison with other major trading partners, Canada's share of U.S. exports was double that of Japan and exceeded that of the ten-nation European Community. At the same time, Canadian exports accounted for 21 percent of U.S. imports. The United States thus has an obvious and substantial interest in Canada's economic prosperity.

United States interest in freer trade with Canada is further substantiated by the following reasons:

1) Increased access to the Canadian market through lowered tariffs and removal of non-tariff barriers at the federal and provincial levels such as: restrictions on U.S. investment in Canada and federal and provincial regulations which impede U.S. services and exports.

   a) Access to the Canadian market is particularly important for U.S. firms that are introducing new products. Integration of the high-per-capita income North American market would reduce the risk of introducing new products and thus enhance the capability of North American-based firms to compete with rivals in Japan and Europe (30, p. 225).

ANALYSIS (CONT.):

D) ADVANTAGES FOR THE UNITED STATES (CONT.)

2) Canada is still the most important location for U.S. foreign investment. Secure, treaty-protected trade and investment relations with Canada would help to create additional security for that investment.

3) The Canadian market offers a substantial opportunity for increased U.S. exports and a reduction of the U.S. trade deficit.

4) Canadian prosperity is desirable to the U.S. because a northern neighbor that is politically unstable, economically depressed, or in a state of social upheaval could develop into a serious worry to U.S. policymakers.

In the Buffalo area alone, the traffic in goods across the Niagara River is now in the hundreds of millions of dollars. Buffalo's situation could change from being a place of economic decline to being at the hub of one of the strongest industrial complexes on the continent.

The negotiation of a free trade area offers the potential for cooperation as a means of putting increased pressure on the U.S. trading partners to open up their markets without the need to resort to import restrictions. As the President's Council of Economic Advisors states:

> "Perhaps most importantly...the possibility of a FTA (free trade area) or, more broadly, multilateral negotiations offers the United States and others the option of using a free-trade instrument, rather than protectionism, as a lever against other countries that are recalcitrant in joining multilateral negotiations" (28, p. 26).

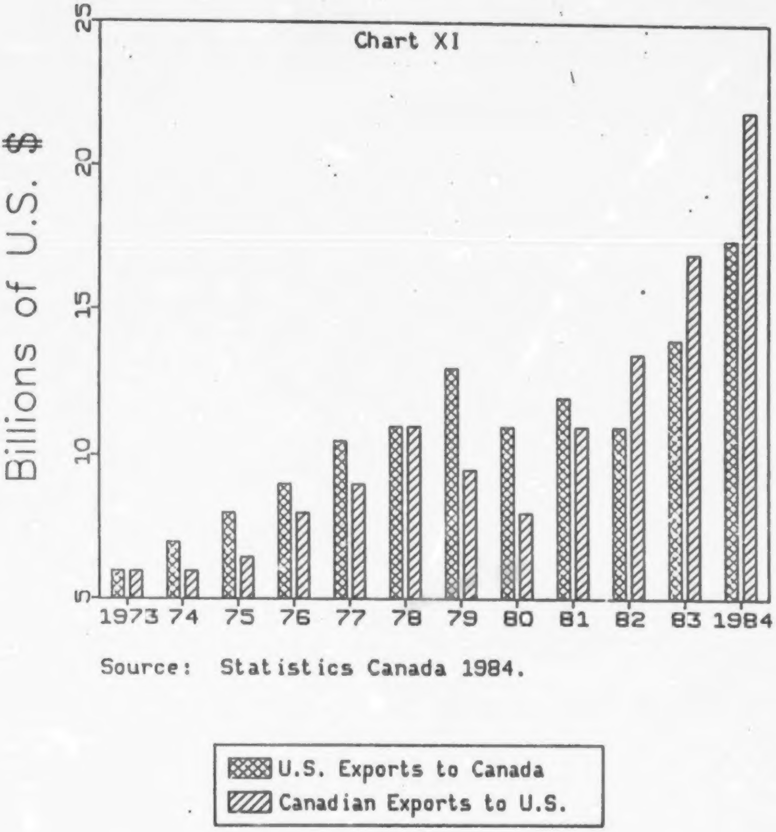
ANALYSIS (CONT.):

E) AN EXAMPLE OF FREE TRADE WITHIN A SECTOR

American automobiles (such as Fords, Chevys, and Plymouths) have been manufactured in Canada for decades; but by the early sixties, Canadians were buying a great many more than they were producing. The problems were manifold. Canadian plants, being small, were relatively inefficient, and each made a wide range of products instead of concentrating on the high-volume production of a few models. A car built in Canada cost more than one built in the United States, and export sales were limited to a few Commonwealth countries. Canadian auto workers' wages were 30 percent below those of American workers (5, p. 7).

The sale of American-built cars and parts in Canada was greatly hindered by tariffs. To resolve their separate problems, the two governments worked out the Automotive Products Trade Agreement. It permitted Canadian industry to establish similar price levels in both countries. The agreement also provides for free trade in all original equipment parts, tires, and batteries (used cars are excluded). It can be terminated by either party with a year's notice, and it is periodically reviewed. The Pact has endured for almost two decades with only minor changes and it almost universally recognized as a success. Automotive trade between the two countries in 1984 totalled U.S. $39.75 billion (Chart XI). In the Buffalo area alone, General Motors has just announced a $340 million improvement of its facilities in the Town of Tonawanda (27, p. C1).

Auto Trade



Source: Statistics Canada 1984.

IV. CONCLUSION

Within the bilateral option, one might try such piecemeal approaches as sectoral free trade agreements and functional agreements on specific nontariff barriers (NTBs). These, however, are likely to produce a minimum of results for a maximum of negotiating effort. The other approach, within the bilateral option, is a comprehensivetrade-liberalizing agreement. The major advantage of the comprehensive over the piecemeal approach is that the negotiations would start with the assumption of providing complete coverage of all merchandise and service trade flows and of eliminating substantially all trade barriers. Exclusions would be permitted only for very special cases.

As Canada and the United States forge policies to cope with changing competitive conditions, each approaches the task from different historical circumstances, with dissimilar assets and liabilities, and with distinctive philisophies about the appropriate role of government. At the same time, by economics and history, there is a link greater than that between any two countries. This situation dictates that the two countries' national interests and policies will at times converge and other times diverge.

The point is that we cannot limit the discussions to trade. If negotiations are going to have any chance of success in the U.S. and Canada, they will have to be inspired by a belief that they transcend bargaining over market shares.

We desperately need a vision wider than protecting existing positions. Both sides need to see that these discussions provide a challenge to reshape relations on this continent as we enter the 21st century - to create a new framework of bilateral economic, political, social, and environmental cooperation.

IV. CONCLUSION (CONT.):

Given the emerging situation in the U.S.and Canada, the prospect of a still more horrific trade deficit, rising unemployment and welling protectionist sentiments - anything less than this just is not going to make it (1, p. 11).

This initiative would not be an act of desperation, but of confidence. A free trade agreement offers the most promising opportunity to create a more efficient, adaptive, and outward-looking Canadian - and U.S. economy that would provide rising living standards and expanding employment opportunities for the great majority of people. Its success would demonstrate to the rest of the world that trade liberalization, rather than rising protectionism, remains - as it has since World War II - the practical key to prosperity.

Chocolate Manufacturers Association
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April 14, 1986

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The Honorable Bob Packwood
Senate Finance Committee
Dirksen Senate Office Building
Room 219
Washington, DC 20510

Dear Chairman Packwood:

The Chocolate Manufactuers Association and the National Confectioners Association together represent 118 companies with 63,000 employees across 32 states. The industry is the second largest industrial user of refined sugar and a major consumer of domestically grown dairy products and peanuts. Industry shipments at the wholesale level last year were $6.6 billion.

American confectionery companies have consistently supported efforts by the Administration and Congress to keep the U.S. market open and free of tariff and nontariff barriers. From this perspective, we support President Reagan and Canadian Prime Minister Mulroney's proposal to establish a bilateral trading relationship free of impediments.

Our exporting companies will benefit immediately from the elimination of Canada's high tariffs on confectionery. However, one major concern we have is caused by the prevailing conflict between domestic agricultural policy and U.S. trade policy. The goal of one is to enhance the competitive environment in the domestic and international marketplace while the effect of the other is to restrict the ability of domestic manufacturers to compete in either one. Unless this conflict is resolved, a major hindrance to free trade between the two countries will remain with U.S. manufacturers at a disadvantage.

In the months ahead, we will work closely with the U.S. Trade Representative and Congress on the U.S.-Canada free trade arrangement while working to improve coordination between domestic agriculture and trade policies, and to minimize risk to the industry while maximizing the benefits of free trade.

Sincerely,

Richard T. O'Connell

Richard T. O'Connell
President

STATEMENT BEFORE THE SENATE FINANCE COMMITTEE CONCERNING THE PROPOSED U.S.-CANADA FREE TRADE ARRANGEMENT

BY

RICHARD T. O'CONNELL, PRESIDENT
THE CHOCOLATE MANUFACTURERS ASSOCIATION OF THE U.S.A.
THE NATIONAL CONFECTIONERS ASSOCIATION OF THE U.S.

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Last year bilateral trade in chocolate and sugar confectionery between the United States and Canada exceeded $100 million and spanned semi-manufactured products through finished sugar and chocolate confectionery packaged for retail sale. Because of the value and scope of confectionery trade, the proposal for a free trade arrangement with Canada has appeal for many segments of our industry.

Canada is the largest foreign market for U.S. confectionery and the elimination of tariffs would immediately assist our exporting companies. Duties in Canada range from 10% on cocoa powder to 12.8% on semi-manufactured and finished chocolate confectionery, to 16% on sugar confectionery. In 1985, the tariff cost on $28.7 million of finished confectionery exports alone was approximately $4.2 million. When the duty is combined with Canada's 12% excise tax on candy, the financial burden on U.S. confectionery competing in that market is substantial.

U.S. duties on the same confectionery categories are zero to a maximum of 7%. Free access to the U.S. market has enabled Canada to become a major supplier of all categories of confectionery from semi-manufactured to finished retail products. (Reference Attachment A)

Despite the benefits of a free trade agreement, we remain concerned about the prevailing conflict between domestic agriculture policy and U.S. trade policy.

Canada has neither a sugar nor milk price support program and its domestic confectionery manufacturers, unlike U.S. companies, buy sugar and milk at world prices. This contributes to a significantly lower cost of production in Canada. The advantage is so profound that half of Canada's confectionery exports to the U.S. are raw and semi-manufactured goods for further processing by U.S. bakery, confectionery and ice cream companies.

High tariffs and the availability of world price sugar and milk in Canada are the prime reasons Canada dominates our bilateral confectionery trade generating 60% of its value. The free trade arrangement will make a major contribution toward correcting the tariff side of the equation.

The disparity in sugar prices which gives Canadian suppliers, and their U.S. customers, a competitive advantage in this market remains the central problem. U.S. sugar prices are likely to be 2 or 6 times the world price for the foreseeable future. Since Canadian sugar prices reflect the world price, U.S. domestic companies manufacturing for home consumption will remain at a competitive disadvantage selling against any imported confectionery made with world price sugar.

The proposed free trade arrangement is an important opportunity to begin to establish a level playing field with Canada in confectionery trade. But the clash between U.S. agricultural policy and trade policy that becomes so apparent in this context can be the real hindrance to free trade. Without a change in agricultural policy, U.S. chocolate and confectionery manufacturers remain at a disadvantage.

The chocolate manufacturing and confectionery industries will continue to support free trade policies and will work with the U.S. Trade Representative and the Congress to eliminate conflicting domestic policies that can undermine the goal of a comprehensive U.S. Canada free trade arrangement.

CWT
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April 11, 1986

COMMENTS ON PROPOSED U.S.-CANADA FREE TRADE NEGOTIATIONS TO THE SENATE FINANCE COMMITTEE

Consumers for World Trade (CWT) is a national, non-profit membership organization established in 1978. CWT supports expanded foreign trade to help promote healthy economic growth; provide choices in the marketplace for consumers; and counteract inflationary price increases. CWT believes in the importance of increasing productivity through the efficient utilization of human and capital resources. CWT conducts its educational programs to keep American consumers informed of their stake in international trade policy and speaks out for the interests of consumers when trade policy is being formulated.

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Consumers for World Trade (CWT) believes that a comprehensive bilateral free trade arrangement with Canada would bring gains to American consumers. We, therefore, favor negotiations to determine whether a suitable agreement can be reached.

The standard argument for free trade is that it will promote American exports to Canada. This a valid argument. It is also true, but almost never stated, that Americans generally also will benefit from the elimination of U.S. tariffs and other border restrictions that now add to the costs of a wide range of Canadian products in our market.

Much of U.S.-Canada trade is already duty free or is subject to low tariffs. This is sometimes taken to mean that few additional gains could come from further reductions in trade restrictions. The fact, of course, is that at present trade in many goods and services is discouraged by relatively high tariffs and other barriers to cross-border trade. Lifting these barriers would make possible a considerably larger exchange of goods and services. The gains from the increased volume of trade would be shared between Canadians and Americans. Over time, these gains should be substantial on both sides of the border.

Our endorsement of a free trade negotiation is subject to two caveats. The first is based on the probability that the negotiators will be under pressure to exempt various categories of products and services from the agreement and otherwise to narrow its scope. To the extent that the final agreement falls short of being comprehensive, its worth will diminish. If the many product areas are carved out and the coverage limited, CWT would hope that the Congress would reject the package as being inadequate.

There is danger that free trade with Canada will cause the two governments to back away from further multilateral reductions in trade barriers. If that were to happen, the potential gains from U.S.-Canada free trade would be overwhelmed by the loss of opportunities for trade expansion on a global basis. This would be particularly damaging to the United States but it would be harmful to the Canadians as well.

As of now, the authorities in Ottawa and Washington have stated their commitment to multilateral trade negotiations under the GATT. A sufficiently comprehensive free trade agreement would be consistent with the GATT's Article 24 and, as the experience of the European Free Trade Agreement shows, need not deter its participants from making mutually beneficial arrangements with other trading partners. CWT suggests that in notifying the President of its decision to grant U.S.-Canada negotiating authority, the Congress should affirm that a bilateral free trade agreement should not limit the right of the United States to exchange trade concessions on a wider basis.

Before the
Committee on Finance
United States Senate

STATEMENT OF THE COMMITTEE TO PRESERVE AMERICAN COLOR TELEVISION (COMPACT) ON THE PROPOSED NEGOTIATION OF A COMPREHENSIVE BILATERAL FREE TRADE ARRANGEMENT WITH CANADA

I. INTRODUCTION

This statement is submitted on behalf of the Committee to Preserve American Color Television ("COMPACT") in connection with the Senate Finance Committee's April 11, 1986 hearing on the President's proposal to negotiate a comprehensive free trade arrangement with Canada. COMPACT is an unincorporated association made up of manufacturers in the domestic television industry and 11 labor organizations which represent the overwhelming number of workers in the domestic television industry. The labor organization members of COMPACT include workers engaged in the manufacture of materials, parts and subassemblies irrevocably destined for incorporation in television receivers and color television picture tubes, as well as workers engaged in the final assembly of color television picture tubes and finished television receivers. A list of COMPACT members is attached to this statement as Appendix A.

Whatever the merits of the proposed arrangement as a general matter, COMPACT believes that free trade with respect to televisions and television picture tubes would not further the international economic interests of the United States but rather, poses the risk of severely injuring the U.S. television and television picture tube industries. In theory, free trade in televisions and television picture tubes would provide both the United States and Canada with certain advantages. In practice, however, the characteristics of the Canadian and U.S. markets in these product areas are such that the benefits of the free trade arrangement would be realized almost exclusively by Canada, and, in particular, by Japanese-owned companies in Canada. The radically disparate size of the Canadian and U.S. television markets will ensure that Canadian television and television picture tube producers will obtain substantially greater benefits from the arrangement than their U.S. competitors. Any export opportunities that the arrangement would create for U.S. television and television picture tube manufacturers would be more than offset by the price suppression and production declines that duty-free imports from Canada would cause.

COMPACT believes that bilateral free trade arrangements are not appropriate where the conditions of trade are such that third countries not party to the free-trade arrangement will benefit. Conditions of trade in the television industry generally, and the structure of the Canadian television and television picture tube industries in particular, make it likely that countries outside the arrangement -- principally Japan -- will receive substantial benefits under the arrangement.

A. The Domestic Color Television Industry is in Poor Health

An examination of the history of the U.S. color television industry and its economic well-being, as reflected in the official findings made in six separate proceedings conducted over a decade and a half by the U.S. International Trade Commission, reveals an industry that has been -- and remains -- extraordinarily sensitive to import competition. The industry has been characterized by consistently low profits since 1979 because of intense price competition, a steady loss of employment, and the proliferation in the United States of final assembly operations by subsidiaries of Japanese, Korean and Taiwanese firms found to have engaged in less-than-fair-value sales. The extension of duty-free treatment to imports of televisions and picture tubes from Canada would pose a serious threat to an industry that the ITC as recently as 1984 found was in a precarious state of health. [1] If such an arrangement were to have any advantages for firms in the United States, it would benefit non-integrated producers maintaining only final assembly operations in the United States at the expense of integrated manufacturers maintaining picture tube production.

In 1960, when imports were an insignificant factor in the domestic market, there were 27 companies participating in the manufacture of television receivers and competing actively for the consumer electronics market. [2] Only 17 remained in 1970; as imports maintained their aggressive market penetration, the number of companies was further reduced to 12 by 1975. [3] Since three of these companies had market shares of less than 0.5 percent, only nine companies with significant percentages of the market remained in the domestic television industry. [4]

While the number of firms producing television receivers in the United States has increased since 1976 to the present level of 19 firms, [5] all but five of these firms are non-integrated final assembly operations. Japanese -- and more recently, Korean and Taiwanese -- participation at the final assembly stage of production has expanded in recent years, primarily because of the threatened enforcement of outstanding dumping orders and orderly marketing agreements applicable to exports from those countries. In 1974, Matsushita Electrical Industrial Co., Ltd. purchased the television

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1/ Color Television Receivers from the Republic of Korea and Taiwan, Inv. Nos. 731-TA-134 and 135 (Final), USITC Pub. No. 1514 at 3, 18 (1984) [hereinafter cited as "USITC Pub. No. 1514"].

2/ Television Receivers, Color and Monochrome, Assembled or Not Assembled, Finished or Not Finished, and Subassemblies Thereof, Inv. No. TA-201-19, USITC Pub. No. 808 at A-8 (1977) [hereinafter cited as "USITC Pub. No. 808"].

3/ See id. at A-9; Television Receiving Sets from Japan, Inv. No. 751-TA-2, USITC Pub. No. 1153 at A-13 (1981) [hereinafter cited as "USITC Pub. No. 1153"].

4/ See USITC Pub. No. 808, supra note 2, at A-8.

5/ USITC Pub. No. 1514, supra note 1, at 7 & n.12.

business of Motorola, Inc., renaming it Quasar Electronics Co.[6/] In 1976, Sanyo Electric Co., Ltd. also began manufacturing televisions in the United States by purchasing the production facilities of Warwick Electronics, Inc., a major private label manufacturer.[7/] Since 1977, Mitsubishi, Toshiba, Sharp, Hitachi, JVC and NEC have also established assembly operations within the United States, along with Tatung and Sampo, Taiwanese-based companies, and Gold Star and Samsung, two Korean companies.[8/] In addition, Wells-Gardner and Curtis Mathes, two American-owned firms, now produce televisions for Teknika (a subsidiary of General Corp. of Japan) and Samsung, respectively.[9/] Today, only five U.S. producers are integrated producers of both color televisions and picture tubes: North American Philips Corp. ("NAPC"), General Electric, RCA, Zenith, and Sony.[10/] General Electric has, however, begun steps to terminate color television production in the United States, and will instead market sets made by Matsushita.[11/] GE will continue to manufacture picture tubes.[12/] In any event, the proposed merger of GE and RCA would reduce the number of integrated producers from five to four. A sixth firm, Toshiba, is scheduled to commence U.S. production of 20-inch flat square tubes sometime this year through a joint venture with Westinghouse.

The attrition of U.S-owned firms over the last 20 years was accompanied by a steady decline in the industry's aggregate profitability. In 1971 and 1972, the industry had pre-tax profits of 8.7 and 8.6 percent of sales, respectively, a profit rate higher than

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[6/] USITC Pub. No. 1153, supra note 3, at A-15.

[7/] Id.

[8/] USITC Pub. No. 1514, supra note 1, at A-9.

[9/] See id. at A-10; Television Digest, Dec. 10, 1984, at 13.

[10/] See Television Digest, May 30, 1983, at 11.

[11/] Id., Oct. 21, 1985, at 10; id., Nov. 18, 1985, at 11.

[12/] Id., Oct. 21, 1985, at 10-11.

U.S. manufacturing in general. [13] Imports totaled approximately 1.3 million units in both 1971 and 1972, and import penetration stood at about 16 percent of the U.S. market. [14] In 1976, however, with imports skyrocketing to approximately 2.8 million units and capturing 33 percent of the U.S. market, [15] industry profits were a mere 3.7 percent of sales; in 1977, profits were only 2.8 percent of sales. [16] By 1978, the profit ratio for the industry was only 1.5 percent, with 1979 and 1980 registering profit rates of 0.8 and 1.9 percent, respectively. [17] Profitability rates for all U.S. manufacturing in the years 1976 to 1980, in contrast, ranged between 8.1 and 6.9 percent, [18] well above profit levels in the U.S. color television industry.

The ITC's 1984 determination in the antidumping proceeding with respect to color televisions from Taiwan and Korea revealed that the industry's financial performance has continued to be unsatisfactory. The firms sampled in this latest investigation recorded operating profits of only 1.2 percent in 1980 and thereafter, registered a profit of 0.2 percent in 1981, a loss of 2.3 percent in 1982, and a profit of a mere 0.8 percent in 1983. [19] These profit rates were significantly lower than those prevailing in related industries and all manufacturing in general during the period. [20] The Commission concluded that the color television industry's financial performance could only be described as "poor," especially in light of the substantial increase in U.S. consumption in 1983. 21/

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[13] USITC Pub. No. 808, *supra* note 2, at A-59.

[14] *Id.* at A-90.

[15] USITC Pub. No. 1153, *supra* note 3, at H-63.

[16] *Id.* at A-53.

[17] USITC Pub. No. 1153, *supra* note 3, at A-53. Note that the cited table erroneously records the 1979 ratio of 0.8 percent as a loss rather than a profit.

[18] *Id.* at A-56.

[19] USITC Pub. No. 1514, *supra* note 1, at A-26.

[20] *Id.*

Data on the industry's financial performance in 1984 and 1985 are unavailable, but it is nearly certain that the industry as a whole registered only minimal profits in 1984 and a net operating loss in 1985. General Electric, Zenith, RCA, and NAPC each announced losses for their consumer electronics divisions in calendar 1985. 22/ It appears unlikely that the industry will be able to return to even marginal profitability in 1986. The U.S. Commerce Department has predicted that the U.S. market for basic consumer electronic products (including television, VCRs and audio equipment) will drop six percent in 1986, primarily because of "exceptionally high inventories and intense price competition." 23/

The decline in profitability and market share has also taken its toll on employment. From a peak of 41,434 production workers in 1973, employment in the industry fell to 24,985 in 1977 24/ and declined further to 21,679 by the first half of 1980. 25/ Further losses in employment occurred in 1981-83, as production and related workers producing color televisions fell to 19,400 in 1981 and 17,572 in 1982 (the year the industry as a whole recorded an operating loss) before increasing marginally to 18,023 in 1983. 26/ That these sharp decreases in employment were not due to improved productivity or technological developments was confirmed by the ITC report in the "escape clause" investigation, which noted that automation-induced unemployment was but a

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21/ Id. at 3, 18.

22/ Television Digest, Jan. 20, 1986 at 16; id. Jan. 27, 1986 at 14; id., Feb. 24, 1986 at 12.

23/ Id., Jan. 13, 1986 at 18.

24/ See USITC Pub. No. 1068, supra note 6, at A-27.

25/ USITC Pub. No. 1153, supra note 7, at A-48.

26/ USITC Pub. No. 1514, supra note 9, at A-21.

fraction of the job losses caused by spiraling imports. 27/ Although the ITC report acknowledged the successful efforts of American manufacturers to increase their productivity, 28/ it pointed out that such gains were more than offset by massive, low-priced imports. 29/

The domestic television industry has experienced severe economic dislocation on account of imports, principally from Japan, Korea and Taiwan. The industry remains in precarious economic condition because of this intense import competition and remains particularly vulnerable to further severe injury if the free trade arrangement with Canada is implemented.

B. The U.S. and Canadian Markets are Very Different

The U.S. market for television and related products is the largest single consumer market for these products in the world. This is a result not only of the relatively large population and high standard of living in the United States, but of the high state of development of the U.S. television industry. Canada, with a population only one-tenth that of the United States, has a significantly smaller television market: while 1985 U.S. apparent consumption of color television receivers for home use was over 16 million units, only about one million color television receivers were sold in Canada last year. Moreover, Canadian television producers probably supplied little more than half of this demand: for example, Canadian color television production in 1982 (a year when the Canadian market was 800,000-850,000 units) was only about 500,000 units. 30/

Despite the small size of the Canadian television industry and the domestic market it serves, Canadian manufacturers have sharply increased their exports of color

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27/ USITC Pub. No. 808, supra note 2, at 19 (views of Chairman Minchew and Comm'rs Leonard and Moore).

28/ Id. at A-48.

29/ See id. at 40 (views of Vice Chairman Parker and Comm'r Bedell).

30/ Television Digest, Oct. 10, 1983, at 19.

televisions to the United States since 1983. In 1983, U.S. imports of color televisions from Canada numbered 86,225 units, while U.S. exports of color televisions to Canada were 206,059, leading to a balance of trade in the United States' favor of 119,834 units. By 1985, however, Canadian exports of color televisions to the United States had risen to 183,204 units, only 21,283 units below the 204,487 color televisions exported by U.S. producers to Canada in 1985. Thus, Canada has managed to increase its exports of color television receivers to the United States sharply over the last three years, while U.S. exports have fallen slightly.

Because of the dramatic differential in the size of the U.S. and Canadian markets, Canada clearly has far more to gain from inclusion of televisions and picture tubes in the proposed free trade arrangement than does the United States. Indeed, for all practical purposes, free trade between the United States and Canada in these product areas would be a one way street, with substantially all of the new traffic moving south. Export opportunities for U.S. producers would be limited, not by tariff barriers, but by the small size of the Canadian market; Canadian producers, on the other hand, would be given free access to the largest national television market in the world. Moreover, as the preceding section demonstrated, the U.S. color television industry can ill afford increased import competition in that market.

There are also important structural differences between the U.S. and Canadian television industries. There are presently 19 firms engaged in producing or assemblying color televisions in the United States. Five of these (Curtis Mathes, GE, RCA, Wells-Gardner and Zenith) are U.S.-owned: one (NAPC) is affiliated with a Dutch company; nine (Sony, Matsushita, Sanyo, Mitsubishi, Toshiba, Sharp, Hitachi, U.S. JVC and NEC) are Japanese-owned; two (Tatung and Sampo) are Taiwanese-owned; and two (Gold Star and Samsung) are Korean-owned. These 19 firms are supplied by four U.S. firms manufacturing picture tubes (RCA, Philips ECG (a subsidiary of NAPC), Zenith and GE), with a fifth firm (Sony) making tubes only for its own needs and a sixth firm

(Toshiba) not yet in production; in addition, a substantial volume of picture tubes is imported. In Canada, on the other hand, there are only five remaining manufacturers or assemblers of color televisions (RCA, Matsushita, Hitachi, Sanyo, and Electrohome/Mitsubishi). The only Canadian manufacturer of picture tubes is Mitsubishi Electronic Industries Canada, which took over the former RCA tube plant located in Midland, Ontario in July 1983.

Thus, the Canadian television industry consists primarily of Japanese-owned firms, while the largest producers in the United States are American or Dutch-affiliated firms. More importantly, Canada's only manufacturer of picture tubes is the subsidiary of a Japanese company, and a very substantial portion of the tubes not produced in Canada are imported from Japan. These corporate and trade relationships make it obvious that Japan has a substantial stake in the proposed United States-Canada free trade arrangement and will receive substantial benefits from it.

II. TELEVISION RECEIVERS SHOULD NOT BE INCLUDED IN THE PROPOSED FREE TRADE ARRANGEMENT

COMPACT believes that inclusion of color television receivers in the proposed free trade arrangement with Canada would be contrary to the interests of the U.S. television industry and its workers. The U.S. television industry is extremely price sensitive, and the significant price advantage that Canadian television manufacturers will obtain under the proposed free trade arrangement would intensify the pressure on U.S. television manufacturers' prices. The establishment of a free trade area would also allow Japanese-owned television manufacturers on both sides of the border to rationalize their production and gain market share at the expense of the integrated television manufacturers in the United States.

A. The U.S. Television Industry is Import Sensitive and Price Competition in the U.S. Market is Intense

The analysis of the health of the U.S. color television industry presented above makes clear that the industry has been peculiarly susceptible to import competition. Moreover, a substantial portion of this foreign competition has not been fair competition; the onslaught of less-than-fair-value imports from Japan that began in the early 1970's has recently been supplanted by dumped imports from Taiwan and the Republic of Korea. These unfairly-traded imports from Japan, Taiwan and Korea have only intensified the price pressure on a U.S. industry that would doubtless be extremely price competitive even in the absence of less-than-fair-value sales.

The extreme price sensitivity of the U.S. color television industry was amply documented in the International Trade Commission's recent investigation in connection with the antidumping proceedings against color television receivers imported from the Republic of Korea and Taiwan. [31] The ITC noted that although U.S. production, shipments, production capacity and capacity utilization increased between 1982 and 1983 in response to a significant rise in U.S. consumption of color TVs, "there was not a corrolative improvement in the financial condition of the domestic producers." [32] Between 1981 and 1983, the industry registered operating profits of less than one percent of sales, with the industry actually recording an operating loss of 2.3 percent in 1982, the industry's worst performance since 1971. [33] The price-depressive effects of imports from Japan, Taiwan and Korea have prevented U.S. television manufacturers from achieving reasonable levels of profit on their manufacturing operations.

In an industry where price competition is so intense that industry profit margins of less than one percent become commonplace, any further intensification of

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31/ USITC Pub. No. 1514, *supra* note 1.

32/ *Id.* at 15.

33/ *Id.* at 15, A-26.

that price competition can be disastrous. COMPACT believes that importers of Canadian televisions would, under the proposed free trade arrangement, realize substantial cost savings that could easily be passed on in the form of lower prices calculated to capture increased market share. An industry subject to price competition as intense as that in the U.S. television industry scarcely needs the competitive challenge of duty-free imports from Canada.

B. Canadian Television Manufacturers Will Obtain a Significant Price Advantage From Duty-Free Treatment

Under the proposed free trade arrangement, a television receiver imported from Canada would, in effect, be treated as a product of the United States from the perspective of the U.S. customs laws. In theory, U.S. television manufacturers exporting to Canada would achieve a greater cost saving under the arrangement than would Canadian manufacturers exporting televisions to the United States; the regular tariff rates for the two countries as of January 1, 1987 will be five percent ad valorem for all televisions imported into the United States and 7.5 percent and 8.2 percent for Canadian imports of 19-inch televisions and other than 19-inch televisions, respectively. Thus, the potential cost savings achievable by U.S. television manufacturers exporting to Canada under a free trade arrangement is greater than that achievable by Canadian firms exporting to the United States.

In the abstract, the concept of sectoral free trade between the United States and Canada has much to commend it. Although the current exchange rate imbalance between the U.S. and Canadian dollars distorts trade by making U.S. products less competitive in Canada and Canadian products more competitive in the U.S. market, the economies of the two countries are roughly comparable in their level of development. As a result, Canadian exports would, in the absence of the effect of customs laws and exchange rates, enjoy no significant competitive advantage in the U.S. market; in general, modestly lower Canadian labor costs would be offset by higher American productivity. This fact suggests that, as between the two countries, one of the oldest rationales for maintaining a "protective" tariff -- the need to equalize the costs of production of imports and domestically-produced goods -- is simply not present. Canadian and U.S.-made goods could compete on roughly equal terms in each national market if tariff barriers between the two countries were eliminated.

Problems with this general scenario begin to emerge, however, where trade involves products not "wholly the growth or manufacture" of the two countries -- that is, where trade in a particular sector has been "internationally rationalized" to a significant degree. This is certainly the case with respect to the manufacture of color televisions. Manufacturers of color television receivers in both Canada and the United States rely heavily upon the use of componentry imported from the Far East and elsewhere. Canadian and U.S. television manufacturers who sell their completed products in their own national markets must pass on to their customers customs duties paid on this componentry. Under the well-recognized rule of duty drawback, however, substantially all import duties paid are refunded to manufacturers on their export sales. This confers a cost advantage on exporters vis-a-vis manufacturers selling domestically. In COMPACT's view, this factor suggests strongly that any bilateral free trade arrangement in a sector (such as televisions) characterized by internationally rationalized manufacturing operations will necessarily place the industry located in the more attractive national market (i.e., the U.S. industry) at a competitive disadvantage.

If the normal principle of duty drawback continues to operate under the proposed free trade arrangement, the suspension of the United States' five percent duty on television receivers imported from Canada will give Canadian producers a substantial competitive advantage over U.S. manufacturers. Canadian producers will get refunds of duties paid on their imported componentry when they export televisions to the United States, and will pay no duty upon entry under the proposed free trade arrangement. These imported televisions would be competing with the products of U.S. producers, who themselves utilize a substantial amount of imported componentry and who must pass on in their selling prices an average duty on those components of four to five percent ad valorem, a sum which cannot be refunded. Thus, the removal of the five percent duty on television imports from Canada will effectively give Canadian producers a tariff advantage over U.S. manufacturers. Canadian producers exporting to the United States will effectively incur no duties, either in Canada or the United States, while U.S. manufacturers selling in the U.S. market will continue to pay duties on their imported componentry.

No sophisticated economic analysis is required to assess the potential effects of this cost advantage. If importers of Canadian televisions choose to pass on the full amount of the duty saving realized under the arrangement, their wholesale prices could be reduced by a full five percent. Such a major price reduction in a market as competitive as the U.S. television market would require a response by U.S. manufacturers. In light of the extremely poor financial performance of the U.S. industry in recent years, such price reductions would be extremely harmful. Certainly, the comparatively paltry market opportunities that the free trade arrangement would give U.S. television manufacturers exporting to Canada would not be enough to offset the strain on the U.S. industry's profitability that increased Canadian competition in the U.S. market would cause.

C. The Proposed Bilateral Arrangement Will Benefit Third Parties, Especially Japan

Because of the structures of the U.S. and Canadian television industries, the proposed bilateral free trade arrangement will necessarily have significant effects for countries outside the arrangement. All of the firms currently manufacturing televisions in Canada are Japanese-owned or affiliated, with the exception of RCA, and each of those companies has an affiliate in the United States. Moreover, it is believed that the Japanese-owned firms in Canada, like their affiliates in the United States, use a relatively greater proportion of imported componentry in their assembly operations. Whether or not Japanese-owned Canadian producers actually increase their use of imported componentry in response to the free trade arrangement, it is clear that any increased sales of televisions by these producers in the United States will inure to the benefit of their Japanese parent companies.

With the advantages of the free-trade initiative, Japanese-owned Canadian television manufacturers will be able to supplement the production of their U.S.-based affiliates. This might involve shifting certain product lines to the Canadian factories, where total costs could effectively be reduced by the effective elimination (via drawback) of duties presently paid on imported componentry. This rationalization of production would increase the general competitiveness of the Japanese firms in North America, and lead to an increase in their share of the U.S. market at the expense of the integrated manufacturers in the United States. COMPACT believes such a result would only lead to further declines in the levels of capital investment and employment in the U.S. television industry.

III. TELEVISION PICTURE TUBES SHOULD NOT BE INCLUDED IN THE PROPOSED FREE TRADE ARRANGEMENT

Duty-free entry of television picture tubes from Canada also poses a significant risk of injury to the U.S. television industry. As the following analysis demonstrates, inclusion of picture tubes in any free trade arrangement with Canada would have extremely adverse consequences for U.S. picture tube manufacturers and by extension, for their affiliated television assembly operations. The direct beneficiary of such an arrangement would be Mitsubishi Electronic Industries Canada, the sole producer of television picture tubes in Canada. Mitsubishi has production capacity far in excess of that needed to service the Canadian market, and is clearly positioned to increase substantially its exports of color television picture tubes to its related subsidiary in the United States, as well as to other Japanese-owned U.S. television assembly companies in the United States. These U.S.-based producers are currently supplied to a substantial degree by U.S. picture tube manufacturers such as Philips ECG, RCA, Zenith and GE. Any decline in the volume sold to this so-called "non-captive" market would have serious repercussions for the cost structures and financial health of U.S. tube producers. A U.S. television industry that has been injured by a decade and a half of low-priced imported televisions can scarcely afford to have the health of its most important productive sector undermined by the ill-advised grant of duty preferences.

A. The Color Picture Tube Industry is Import Sensitive

A color television receiver is comprised of many highly complex components. The picture tube is the most sophisticated. The housing of this tube is typically a funnel-shaped vacuum glass envelope or bulb. In the case of most tubes, three electron guns, situated at the narrow end of the funnel, are aimed toward the display screen at the opposite end. The back surface of this display screen is coated with red, blue and green phosphor dots or stripes which are excited by the stream of electron beams put out by the electron guns to produce multi-color images.

The color picture tube is by far the most expensive component of the television receiver. It is estimated that the typical color picture tube accounts for approximately 45 percent of the cost of materials and 25 percent of the cost of the completed set. This high cost is explained by the fact that color picture tube production facilities are extremely capital intensive and have high fixed costs. It is estimated that an investment of $75 million is currently required to establish a new U.S. facility to manufacture color picture tubes, an investment that can be recovered only by high rates of capacity utilization, normally involving a five-day per week, three-shift per day operation. As a result of this capital intensity and high fixed costs, the "break-even" point in tube production is relatively high. Thus, the volume of production is a critical factor in tube production profitability. Even marginal losses of production volume can raise serious questions as to the viability of continued operations.

There are presently only five producers of color picture tubes in the United States -- Philips ECG, General Electric, Zenith, RCA, and Sony; a sixth firm -- Toshiba -- is to commence production in the near future. All of the current manufacturers except Sony service the non-captive market in addition to supplying affiliated television set manufacturers. The glass envelopes or bulbs used in making these picture tubes are manufactured by three firms -- Owens-Illinois, Corning Glass Works, and RCA.[34] Glass envelope production is also extremely capital intensive and requires high rates of capacity utilization to maintain profitable operations.

B. Conditions in the U.S. Color Picture Tube Market

As the preceding discussion makes clear, full utilization of production capacity is critical for color television picture tube manufacturers. Nevertheless, world capacity to produce color television picture tubes is currently estimated at about 70 million units, substantially above worldwide demand. Moreover, new picture tube plants are in the process of being built in Korea and the People's Republic of China that could increase worldwide capacity by an estimated 20 million tubes per year.[35]

Although U.S. color television picture tube production capacity is sufficient to meet the needs of the U.S. market, the overcapacity of the picture tube industries in various foreign countries has caused U.S. color television picture tube imports to nearly triple since 1982. Moreover, combining the effects of imported color television receivers and imported picture tubes, the percentage of television sets sold in the United States which had foreign picture tubes increased from approximately 27 percent in 1982 to 48 percent in 1985.

This massive surge is partly explained by the chaotic trend in picture tube pricing in the U.S. market. In 1980, the average price of a 19-inch color picture tube was

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34/ Television Digest, Aug. 13, 1984, at 13.

35/ Prepared Statement of Jerry K. Pearlman, Chairman and President, Zenith Electronics Corp. in support of H.R. 2349 at 3 (submitted to the Subcommittee on Trade of the House Ways and Means Committee on February 6, 1986).

about $80.00; the average price was approximately $65.00 in 1985, despite an increase in material costs over this five-year period. 36/ This price decline corresponds with the surge of color television picture tube imports since 1980, and reflects the extreme pricing pressure characterizing the present picture tube market.

Despite a color television sales increase in the U.S. market in 1985 of 500,000 units, U.S. production of color picture tubes fell by 1.8 million units. In his testimony before the Subcommittee on Trade in February, Mr. Jerry Pearlman, Chairman and President of Zenith Electronics Corp., put the net loss to U.S. picture tube manufacturers in graphic context:

> These 2.3 million lost units represent the output of one fair-sized color picture tube plant in the U.S. industry. The loss is roughly equivalent to Zenith's tube production in 1985. It was roughly the capacity of the North American Philips Seneca Falls, New York, tube plant that was closed last year. The impact was spread among four companies: Zenith, RCA, Philips and GE. Had it all been at Zenith, the impact would have been all 2,200 jobs in our picture tube business. The impact in pre-tax profit to U.S. tube makers was about $50 million. 37/

A number of factors make it extremely likely that U.S. color picture tube manufacturers will be confronted with reduced sales volume -- and consequently, a dangerous situation of overcapacity -- over the next few years. First, imports of color picture tubes show every sign of continuing to increase, despite the current 15 percent duty on U.S. tube imports. Between 1984 and 1985 alone, color picture tube imports rose from 792,744 to 1,701,015, or by 115 percent. These figures represent a quantum jump above the level of color tube imports during the late 1970's; import levels in the period from 1977 to 1979, for example, were fairly stable and averaged 312,000 units. The surge in imports began with smaller screen size tubes and has become so overwhelming in recent years that for all practical purposes, U.S. picture tube manufacturers have aban-

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36/ Id.

37/ Id. at 5.

doned the small-size tube market. Foreign tube producers have now begun to focus on exporting the larger, more profitable screen sizes above 13 inches in diameter. Figuring prominently in this increase in larger tube imports has been Canada's Mitsubishi, which doubled its exports to the United States of tubes 19 inches and over between 1984 and 1985, from 106,158 to 229,341 units. Indeed, in 1985, Canada supplanted Korea as the largest foreign supplier of 19-inch color picture tubes. Thus, the current surge in tube imports is focusing on the most profitable market segment for U.S. tube producers, particularly with respect to their production for the non-captive market, and Canada is a leader in the assault.

Another additional factor that will likely reduce demand for U.S.-made picture tubes in the next few years is continuation of the increase in imports of complete and incomplete color television receivers with picture tubes. Between 1983 and 1985, imports of complete color televisions (including kits) rose by 77 percent, increasing from 5,268,228 to 9,327,485. Within this category, kits imported from Mexico rose from 448,661 units to 661,530 units, or by 47 percent. Imports of incomplete receivers containing picture tubes have exceeded this trend. Imports of incomplete receivers with a picture tube increased from 90,932 in 1983 to 432,518 in 1985, or by 375 percent. This indirect pressure on U.S. color picture tube manufacturers caused by increased imports of complete and incomplete color televisions, which displaces demand in the United States for color picture tubes used in domestically-produced televisions, is compounding the direct pressure exerted by imports of color picture tubes, and will probably intensify in the future.

In light of this outlook for the longer term, it appears that any proposal that would tend to increase the supply of imported picture tubes in the U.S. market would pose a significant risk to the health of U.S. picture tube manufacturers. The 15 percent U.S. duty on picture tubes has been a critical factor in limiting import competition in the U.S. picture tube market and must be maintained as against all foreign sources if U.S.

picture tube manufacturers are to maintain the high levels of capacity utilization needed to operate profitably.

C. Mitsubishi Electronic Industries Canada Will Displace U.S. Tube Manufacturers as Suppliers of Japanese-Owned U.S.-Based Television Assemblers

The chief beneficiary of any arrangement under which television picture tubes could pass duty free between Canada and the United States would be Mitsubishi Electronic Industries Canada, the sole picture tube manufacturer in Canada. U.S. tube manufacturers have made, and will doubtless continue to make, a modest amount of sales in the Canadian market, but the dramatic disparity between the size of the U.S. and Canadian markets will clearly give Mitsubishi the better half of the bargain. Moreover, Mitsubishi will find a ready market in the United States for its products not only in its related subsidiary, Mitsubishi Consumer Electronics of America, Inc., but also in sales to the other non-integrated television assemblers in the United States, most of which are Japanese-owned.

Since commencing operations in 1983, Mitsubishi has demonstrated its ability and intent to increase its exports of picture tubes to the United States. Operating out of a plant in Midland, Ontario acquired from RCA for approximately $16 million in July 1983, Mitsubishi immediately upgraded the facility with approximately $12 million in financial assistance received from the Canadian federal and Ontario provincial governments. 38/ Mitsubishi is reported to have produced approximately 750,000 picture tubes in 1984. 39/ In April 1985, the firm was reported to be awaiting approval from Mitsubishi of Japan of a plan to expand its production capacity at the Ontario facility by 50 percent to 1.5 million picture tubes annually. 40/ Output is believed to be restricted currently to

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38/ Id., July 11, 1983, at 12.

39/ Id., April 1, 1985 at 14.

40/ Id.

19- and 25-inch color picture tubes, but the planned expansion would involve retooling for manufacture of 20- and 27-inch square-cornered picture tubes. [41]

U.S. import statistics show a dramatic resurgence in U.S. imports of color television picture tubes from Canada in 1984 and 1985. In 1983, the year in which Mitsubishi assumed control of the idled RCA facility, U.S. imports of picture tubes from Canada numbered only 7,267, and the United States had a surplus in picture tube trade with Canada of 278,848 units. In 1984, by contrast, 106,200 color television picture tubes were imported from Canada, about double the average prevailing between 1978 and 1980, and the U.S. surplus fell to 206,508 units. By 1985, Mitsubishi's exports to the United States had more than doubled to 229,418, and the U.S. picture tube trade surplus had changed to a deficit of 21,551 units.

The effect of this increase in imports, however, cannot be fully appreciated by examination of the numbers alone. More importantly, there has been a dramatic shift in the nature of Canadian television picture tube exports to the United States. As noted above, Canadian picture tube exports to the United States averaged about 50,000 per year between 1978 and 1980. Exports during this period represented shipments by RCA of Canada to RCA of the United States, which is itself an integrated manufacturer of both picture tubes and completed televisions; hence, the sales were basically intra-corporate transfers within the captive market for color television picture tubes. Mitsubishi's exports to the United States since 1983, however, have been primarily to Mitsubishi Consumer Electronics America and Sharp Electronics, firms accounting for a substantial portion of the U.S. non-captive market for color television picture tubes.

Clearly, if Mitsubishi of Canada has found it possible to transform a large picture tube trade surplus in favor of the United States into a surplus in favor of Canada in only its second year of operation, notwithstanding the substantial 15 percent import duty, its volume of exports under a free trade arrangement would increase significantly. The availability of Canadian picture tubes at prices reflective of duty free treatment would almost certainly win Mitsubishi of Canada a number of Japanese-owned U.S.-based television assembler customers in addition to Mitsubishi of the United States and Sharp. With the Canadian subsidiaries of Hitachi and Sanyo already purchasing tubes from Mitsubishi, the U.S. subsidiaries of these companies would seem especially likely candidates for turning to Mitsubishi of Canada for all or part of their picture tube needs. If these firms and the other Japanese-owned U.S. television assembly facilities turn to Mitsubishi for all or a significant portion of their picture tube needs, the non-captive picture tube market in the United States would virtually disappear. Zenith, NAPC, RCA and GE depend on sales to the non-captive market to maintain critical production volume and capacity utilization rates. The closing of one or more picture tube facilities by these integrated producers would almost certainly be required to address this dramatic reduction in tube demand. The result would be severe injury to the U.S. television industry and its workers.

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[41] Id.; see also id., July 16, 1984 at 11.

IV. CONCLUSION

COMPACT strongly believes that the proposed free trade arrangement should not include televisions or television picture tubes. Half a dozen determinations of the International Trade Commission over the past 15 years have documented the extraordinary import sensitivity of the U.S. television industry. This is a sui generis industry that cannot afford to be exposed to totally free trade from any source.

The structures of the Canadian and U.S. television and television picture tube industries and markets assure that the Canadian industry would obtain substantially greater benefits than U.S. firms would under any free trade arrangement. The large American television market would give Canadian television producers opportunities that would make those offered by the Canadian market pale in comparison. The Japanese ownership of most of Canada's television manufacturers would also give them an incentive to work closely with Japanese-owned U.S. television manufacturers in an effort to maximize their shares of the U.S. market at the expense of the non-Japanese participants in the industry. Finally, inclusion of television picture tubes in the free trade proposal would provide the greatest benefits to Canada's sole manufacturer of picture tubes, Mitsubishi Electronic Industries Canada. Mitsubishi has made a substantial capital investment in its plant, and possesses production capacity far in excess of that justified by consumption levels in Canada. Any action that would tend to direct that capacity toward the U.S. market could only undermine the health of the U.S. picture tube industry, and with it, the television industry on which it depends.

Respectfully submitted,

COLLIER, SHANNON, RILL & SCOTT

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April 10, 1986

UNITED STATES SENATE
COMMITTEE ON FINANCE

COMMENTS REGARDING PROPOSED U.S. - CANADA FREE TRADE NEGOTIATIONS AND THEIR POTENTIAL IMPACT UPON THE U.S. BICYCLE INDUSTRY

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APRIL 21, 1986

Introduction

The Cycle Parts and Accessories Association ("CPAA"), located in New York City, is a national trade association whose membership comprises the leading U.S. producers of bicycle components. In previous submissions to this committee, we have described the serious plight of our members and their major customers, the U.S. bicycle manufacturers.

Allow us to update information previously furnished with these brief statistical notes:

- U.S. parts makers continue to suffer through some of the worst times in the history of this industry. Total membership in CPAA has declined 50% over the past five years as company after company has been driven out of business.
- U.S. parts manufacturers continue to suffer an erosion of their market share, now estimated at less than 25%....and declining still.
- It is estimated that total employment by U.S. parts manufacturers has declined by more than 50% in the last five years. Nor is the prognosis very good for an upturn in employment as members continue to retrench and curtail their operations.

- The situation faced by U.S. bicycle manufacturers is equally bleak. Their market share has dropped from 83% in 1979 to 51% in 1985.
- Total employment by domestic bicycle manufacturers has experienced a similar decline.
- Some bicycle manufacturers have gone totally off shore while others continue to retrench, cutting their costs to the bone.

Against this background, you might expect us to be extremely wary of a proposed free trade zone between our country and Canada.....and indeed we are. However, for the reasons hereinafter enumerated, we do not feel that the concept should be dismissed out of hand and we ask that your committee allow the talks to proceed.

In saying this, we presume that there will be ample opportunity to provide input at various stages of the negotiation process prior to the signing of a formal treaty with Canada.

Trade in Bicycles and Parts Between the U.S. and Canada

The amount of trade in both bicycles and components between the United States and Canada is minimal. During 1985, only 117 bicycles were imported from Canada, a miniscule percentage of the

6.6 million units that entered this country, mostly from the Far East. During the same period, only 34 bicycles were exported to Canada.

The situation was much the same with bicycle parts. The dollar volume of imports from Canada totalled only $136,290, again, a miniscule percentage of the $139,000,000 worth of parts that entered the United States during that period.

Considering the fact that the United States and Canada share such a large border in common with numerous crossing points enhanced by excellent internal transportation systems, the miniscule amount of trade in bicycles and parts is almost hard to believe. This may present an opportunity for U.S. parts manufacturers. Perhaps there is a potential for growth in trade with our neighbor to the North. It is certainly worth looking into.

Potential Benefits to Parts Manufacturers

A few members of our association have already investigated opportunities in Canada and what they report back gives us reason for encouragement. One member formed a joint venture with a Canadian company to produce bicycle parts in Canada. The relationship seems to be working well, notwithstanding the inordinate amount of red tape and the tariff wall between the two countries which discourages two way trade. For this member, a U.S. - Canada free trade agreement would be a boon to its business.

Still another member owns and operates a parts manufacturing facility in Canada. For many of the same reasons, this member also strongly supports a free trade agreement.

But it is not only the members who have already invested in Canada that support a free trade agreement. Other members with no present investment stake are also supportive of a free trade agreement. For them, Canada represents another market for their goods as well as a potential source of low cost raw materials for their manufactured products. In short, a free trade agreement with Canada would put U.S. manufacturers in a preferred trading position with Canada vis a vis other countries.

Risk Factors

Free trade, however, is a two way street and there is a certain amount of "downside risk" associated with our support of a free trade agreement with Canada. Ranking high on the list of risk factors would be the double whammy impact of an exceptionally low Canadian dollar and the lower wage scales that prevail there. We have witnessed what these factors have done to the lumbermen in Washington and Oregon and would not want the same fate to befall us.

Nonetheless, these two factors have prevailed for quite some time. The only difference with a free trade zone would be the elimination of duty and it is our belief that just by adding this one new factor, we are not likely to experience a flood of imported bicycle components, similar to what we have been forced to endure from Taiwan, Korea and other countries of the Far East.

At present, Canada does not have the capacity to become a major parts manufacturer and the elimination of duty alone is not likely to induce a significant redeployment of capital investment into the manufacture of bicycles and parts. Thus, while we fear competition from Canada, the Canadians probably have as much reason to fear competition from us.

Another concern we have is over transshipment through Canada of merchandise actually manufactured in the Far East. Any free trade agreement with Canada must contain adequate protection, similar to those in the Caribbean Basin Initiative and the GSP Program, in order to guard against this. It is not such a problem for our industry because most of the Canadian tariff rates on bicycle parts from the Far East are higher than our own so there would be no benefit to be derived from transshiping merchandise through Canada. However, this could be a serious problem for other industries.

Conclusion

For all of these reasons, we believe that a free trade zone with Canada would benefit us more than it would hurt us. However, this is only a preliminary determination. The Reagan Administration has provided us with scant information regarding its goals and objectives in these proposed negotiations with Canada. Accordingly, we cannot make a final determination of how a free trade agreement will affect our industry until we see how the negotiations progress. We respectfully reserve the right to file additional comments once the picture becomes clearer as to exactly what our country is seeking and what it is prepared to give up.

Under §102 of the Trade Act of 1974, as amended by §401 of the Trade and Tariff Act of 1984, the President has authority to enter into bilateral negotiations with Canada unless the House Committee on Ways and Means or the Senate Committee on Finance disapproves of such negotiations within sixty legislative days after being so notified. While we respectfully reserve the right to comment further regarding the substance of these negotiations, for now, we believe that these negotiations are in the best interest of our industry and the United States. Accordingly, we urge the Committee on Finance to allow these talks to proceed.

Respectfully submitted,

Cycle Parts and Accessories Association

By: Robert Auerbach
Robert Auerbach, General Counsel

COMMENTS OF FLORIDA CITRUS MUTUAL CONCERNING THE PROPOSED U.S.-CANADA FREE TRADE AREA

These comments are filed on behalf of Florida Citrus Mutual, Lakeland, Florida ("FCM"), in connection with the invitation of the Subcommittee on Trade for comments concerning the proposed negotiations between the United States and Canada on the formulation of a bilateral free trade area. FCM is a voluntary cooperative association consisting of 12,936 growers of citrus for processing, as well as processors of citrus fruits.

FCM takes no position at this time with respect to the desirability of entering into a bilateral free trade arrangement between the United States and Canada. However, any bilateral free trade agreement should include Country of Origin requirements which prevent abuse of the Free Trade Area through the transshipment of products which are not articles of either country, or are not substantially transformed in either country. The existence of duty free treatment may provide an incentive to marketers of numerous products to avoid duties through transshipment of articles of third country origin, with minor processing operations performed in one of the free trade area countries. FCM strongly believes that any U.S.-Canada agreement should include specific provisions designed to establish strict and enforceable country of origin criteria.

The Congress has recognized this concern previously with respect to the Free Trade Area (FTA) agreement with Israel and in the legislation establishing the Caribbean Basin Economic Recovery Act. The U.S.-Israel Free Trade Agreement, enacted by Public Law 99-47, 99 Stat. 82, 99th Cong. (1985), requires that an article may only become eligible for duty free treatment when imported into the United States if it is (a) wholly the growth, product, or manufacture of Israel or is a new and different article of commerce that has been grown, produced or manufactured in Israel, and (b) the sum of Israeli materials plus direct processing costs performed in Israel is 35% of the appraised value. The Agreement provides specifically that "no article shall be considered a new and different article of commerce under the Agreement and no material shall be eligible for inclusion as domestic content under the Agreement by virtue of having merely undergone a) simple combining or packaging operations, or b) mere dilution with water or with another substance that does not materially alter the characteristics of the article or material." See, Note 2, Agreement on the Establishment of a Free Trade Area Between the Government of the United States of America and the Government of Israel (1985).

Provisions similar to those included in the U.S.-Israel FTA appear in the Caribbean Basin Economic Recovery Act

(CBERA). The law requires that in order to be eligible for duty free treatment under the CBERA, an article must be wholly the growth or manufacture of a beneficiary country and may not be eligible for treatment "by virtue of having merely undergone (A) simple combining or packaging operations, or B) mere dilution with water or mere dilution with another substance that does not materially alter the characteristics of the article." Public Law 98-67, Section 213(a)(2)(A) and (B) 1983). These restrictions have been incorporated into regulations of the U.S. Customs Service concerning eligibility for duty free treatment under the CBERA.

Under current U.S. law, mere processing, such as the reconstitution of orange juice from frozen concentrated orange juice, does not constitute "substantial transformation" of the product for purposes of marking the country of origin under Section 304 of the Tariff Act. See, Customs Ruling CSD 85-47, September 4, 1985. Reconstitution of orange juice is precisely the type of manipulation intended by Congress in the CBERA and the U.S.-Israel Free Trade Area not to qualify a product as an article of a beneficiary country for purposes of obtaining duty free treatment. See, H. Rep. No. 98-266, 98th Cong. 1st sess. 13 (1983). In this regard, FCM notes that Canada has no indigenous production of oranges or orange juice, and therefore, could not be a supplier of FCOJ to the United States. Presently, some FCOJ imported into Canada from Brazil, Mexico, or other third countries is processed and may be exported to the United States. The provisions of any U.S.-Canada Free Trade Area should clearly indicate that such product will not be eligible for duty free treatment by reason of having undergone such insignificant processing operations in Canada.

In conclusion, FCM strongly believes that any free trade area negotiated between the United States and Canada should guarantee the true benefits of bilateral duty free trade by specifying strict country of origin rules in order to avoid the contravention of these intended benefits.

Respectfully submitted,
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April 10, 1986

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April 3, 1986

STATEMENT OF THE
INLAND FOREST RESOURCE COUNCIL
TO THE
COMMITTEE ON FINANCE, U.S. SENATE
ON THE MATTER OF A
FREE TRADE AGREEMENT BETWEEN
THE UNITED STATES AND CANADA
APRIL 11, 1986

The Inland Forest Resource Council is an organization of forest product manufacturers in Montana and northern Idaho. Council members produce wood products, particularly lumber, in direct competition with Canadian sawmills. They also make products that today are virtually excluded from Canadian markets by tariffs.

Canadian Lumber Imports

Lumber manufacturers in Montana and northern Idaho produce the same lumber product as sawmills in interior British Columbia - Spruce, pine, fir (SPF) dimension. These companies should be able to compete head to head with the Canadians in U.S. markets and win the order most of the time. The species offered is the same, the quality is the same or better, and manufacturing and shipping costs are competitive. Yet Canadian producers consistently undersell Idaho and Montana mills in their markets. Why? The Canadians have two advantages - one is in the exchange rate and the other is in stumpage pricing.

Exchange Rate

There is no question that recent Canadian/US exchange rates of $.65-$.70/$1.00 give some advantages to Canadian importers into the U.S. This is true not only for lumber but for hogs, natural gas and other resources. Even when the higher inflation rate in Canada is taken into account, some advantage remains.

Recently, the U.S. dollar has declined in value substantially against other major world currencies - except the Canadian dollar. Canadian/U.S. exchange rates remain firmly rooted where they have been for months. It is not reasonable to expect this to occur, and it strongly suggests that the Canadian government is manipulating the current markets to maintain an exchange rate favorable to Canadian exporters in their biggest market, the U.S. If this is the case, and the committee is urged to investigate it, it amounts to a trade subsidy just as surely as if the Canadians were providing free transportation for their goods into the U.S. Because manipulation of the exchange rate influences all aspects of trade, the committee should insist that this subject be included in negotiations.

Stumpage Pricing

Stumpage prices, the cost of standing timber, are an important factor in the competitive equation. The facts clearly show that timber is provided to Canadian mills at less cost than to U.S. mills, particularly those U.S. mills that depend on timber from the national forests. Much of this is due to the fundamentally different way timber is priced in the two countries.

National forest timber in the U.S. is sold at auction to the highest bidder. A minimum bid price is set as the fair market value at the time the timber is sold. Since most national forest timber is not cut for two or three or more years following its sale, prospective purchasers must speculate on the fair market value at the time of harvest and bid accordingly. Many times purchasers are forced by restricted availability of national forest timber to bid higher than they might normally just to ensure a supply of raw material.

Only in British Columbia does timber pricing approach that of the national forests; i.e., bidding; but the bids are for long term licenses. In other provinces, stumpage prices are set arbitrarily without the slightest regard for the market. Since virtually all timberland is controlled by the provincial governments, there is little competition and ample opportunity for stumpage to be supplied at less than market value.

To date, there has not been adequate investigation of this possibility. It is clear that the price advantages obtained by Canadian producers cannot be totally accounted for by the exchange rate. Since production efficiencies are similar and transportation costs competitive, the additional advantage can only be coming from subsidized stumpage.

Legislation now pending before Congress, known as the Gibbons-Baucus Bill, will allow the International Trade Commission to investigate the possibility of natural resource input subsidies. The alternative to such an investigation will be for the Canadian government to negotiate a resolution of the lumber import issue. In any event, the lumber import problem must be dealt with either through negotiation or legislation and subsequent investigation before general talks on a free trade agreement proceed.

Ultimately a free trade agreement will be in the best interest of both countries, but such an agreement must be based on the principles of fair trade - no exchange rate manipulation, no subsidized natural resource inputs. The best place to establish these principles is through resolution of the lumber import issue.

Canadian Tariffs

While Canadian lumber producers have free access to U.S. markets, the Canadians have imposed tariffs on other wood products coming into that country.

An example is certain types of millwork. A plant in Missoula, Montana, manufactures window and door frames from ponderosa pine, a species not prevalent in Canada. Stiff tariffs are placed on imports of this type of product into Canada, yet Canadian plants must import proper lumber from the U.S. to serve the market. This is not an efficient approach.

If these tariffs were removed through a free trade agreement, U.S. mill work manufacturers could supply the Canadian market more efficiently while increasing production and jobs in this country.

In summary, there is a lot of unfair trade going on between the U.S. and Canada, and it is all to the advantage of the Canadians. If the Canadians are going to subsidize their lumber industry through exchange rate manipulation and subsidized stumpage, then free trade cannot occur. These issues must be resolved before broader free trade discussions go forward.

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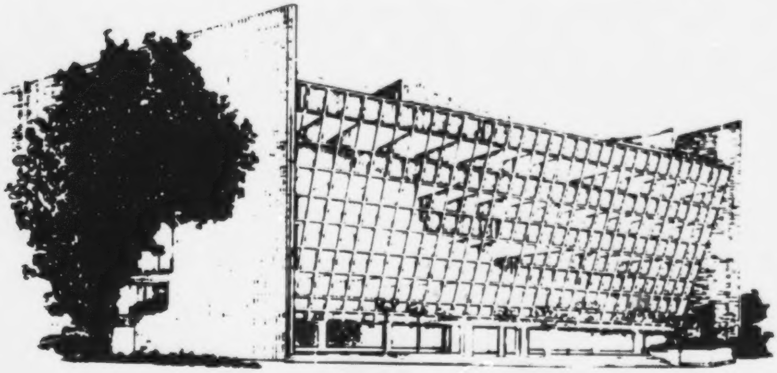
Statement of the NATIONAL ASSOCIATION OF HOME BUILDERS before the

Committee:	Senate Finance Committee
Subject	Bilateral Negotiations
Witness	David C. Smith
Date	April 11, 1986
Place:	215 Dirksen Senate Office Building



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On behalf of the National Association of Home Builders (NAHB), a trade association representing 138,000 members, I am respectfully submitting a statement for the record on the proposed initiation of bilateral negotiations between the United States and Canada on a comprehensive free trade arrangement. NAHB supports a free trade agreement between the two countries including unrestricted trade on Canadian softwood lumber imports.

As home builders, we are by no means experts on all of the complex issues of international trade. However, we have an interest in long-term economic growth and world-wide U.S. competitiveness. Retaining and increasing American jobs and maintaining competitive costs for the long-term is something which will benefit not only home builders, but consumers and the domestic economy as well. And it is within this larger picture that we view the mounting trade deficit and the proposals to restrict Canadian softwood imports.

Recent trade debate seems to have focused on those countries which impose barriers to "free trade". This is not the case with Canada. The United States and Canada have traditionally had a special relationship, and they are each other's best customers in international trade. In 1984, the total trade between Canada and the United States amounted to over $120 billion in U.S. dollars. In fact, the Canada-U.S. relationship is the largest exchange between any two nations in the world. The United States does more trade with Canada than it does with Japan; more with Ontario than with the European Community; more with British Columbia than with China. American investment in Canada represents some 80% of all foreign capital in Canada, and 25% of all U.S. investment abroad. Conversely, Canada is the fourth largest foreign investor in the U.S..

Our economies grow together. Even with the current U.S. trade deficit, trade with Canada still brings net jobs and advantages to the United States. Canada is the fastest growing foreign market for the United States. The trade of New York State with Canada in 1984 was over $15 billion, a figure larger than all U.S. trade with France. The question we pose is relatively simple-- Do we want to encourage growth in this arena, or do we want to protect ourselves from bilateral growth?

The U.S. imports $350 billion worth of goods a year; Canada's share of U.S. imports is only 20 percent. While each country could indeed go elsewhere with their exports-- and perhaps the opportunity for growth could well be greater in other directions -- NAHB believes for a variety of reasons that our trade with Canada should be encouraged and even further developed.

In 8 of the last 11 years, the U.S. has enjoyed a trade surplus with our trading partner to the north. But we are concerned that recent legislation to restrict Canadian timber threatens this historical relationship. If protective legislation is passed, we fear the result eventually would be to undermine both the U.S. exports to Canada and the U.S. economy in future internationally competitive situations.

Canadian Softwood

NAHB strongly supports free trade for Canadian timber products. Some contend that the differences between U.S. and Canadian prices for timber are the result of subsidization. However, the allegation of subsidy was exhaustively debated and dealt with by the International Trade Commission (ITC) in 1982. In 1983, the Department of Commerce concluded that no significant subsidy existed.

The speculation about a subsidy came about for several reasons. Some American lumber spokesmen have claimed that the rise in Canadian lumber imports has been spectacular and have cited the fact that the Canadian share of the U.S. market increased from 19 to 32 percent between 1975 and 1984. In looking at overall American exports and imports, sharply varying conclusions can result, depending on the base year chosen and other input variables. The Canadian share of U.S. timber consumption in 1975 was uniquely low because the industry was hit by labor strikes pushing production far below normal. The Canadian industry's production and its share in the U.S. market returned to historical norms in 1976 and 1977. The ITC report used Canadian production in more normal years to measure change, and their findings concluded that the Canadian share has shown only a modest increase. According to the ITC report, the Canadian share increased from 28 percent in 1982 to 29 percent in 1984, a gain of one half a percentage point a year. In addition, the growth closely paralleled the increasing strength of the U.S.

dollar, which currently gives Canadian lumber at least a 35% advantage over the U.S. dollar.

Many differences between the two countries create a difference in stumpage prices. Moreover, direct comparisons between prices paid for stumpage in the two countries and the delivered cost are very difficult to make. For instance, Canada has an abundance of forest resources while the U.S. has little surplus. Perhaps surprisingly, many Canadian mills are more advanced technologically than their U.S. counterparts.

Species mix and species preference between the U.S. and Canada are difficult comparisons to make. The largest and most productive forests in both countries are found in the far west. In 1984, 44% of the trees harvested in Washington and Oregon were Douglas fir, a relatively valuable species. In British Columbia, which is Canada's largest timber producing region, Douglas firs accounted for only 9%.

The different characteristics of different species and the difference in the quality of millwork of the same species in different localities make comparisons of general prices difficult at best and often impossible.

The initial costs in the lumber industry are defined as the cost of the trees and the costs of cutting and delivering them to the mill. For example, a large tree on a parcel of land adjacent to a sawmill is worth considerably more than a second, identical tree on a parcel 1,000 miles from the nearest sawmill. In the case of the first tree, the mill owner must simply cut the tree and haul it next door to be manufactured into lumber. In the case of the second tree, the millowner must cut the tree, and then pay to transport it 1,000 miles before it can be utilized. The cost of transporting the log from the second tree directly reduces the value of the tree and, accordingly, leads to a perfectly justifiable difference in the price of the first tree and the price of the second tree.

Transportation costs are only one of several factors that affect the value of standing timber. Forest industry economists explain that the value of timber is nothing more than the value of the end products (lumber and wood chips), less the costs of logging the timber; transporting the logs to mill; manufacturing the end products; and transporting the end products to market. Factors which affect these costs include the species and size of the timber, the topography and climate of the area in which the timber is located, the proximity of that area to a sawmill,and the proximity of the mill to end-product markets. Thus, the value of timber includes more than the price of the standing tree. In fact, U.S. Forest Service information shows the variation in stumpage prices within the United States to be just as great as the variation between the U.S. and Canada. While it is true that the stumpage prices in Canada are lower than in the U.S., the existence of such price differences does not necessarily constitute a subsidy.

Almost all of Canada's productive forests are publicly owned. The governments lease their land on long-term contacts.

In return, the leaseholder assumes many of the costs of road building, reforestation, and forest management. Overall, Canada has a relatively large supply of timber available to a relatively small market. There are 544 million acres of productive Canadian forest, some 61 million acres more than the United States, even though Canada has only one-tenth of our population.

In the U.S., public lands constitute only about a third of the forest, yet they contain 63% of the softwood timber. U.S. public lands are considered to be the least productive because timber cutting on them is held to about 10 billion board feet a year as a matter of public policy.

Timber from U.S. government land is first appraised and then open to competitive bids. The auction bids are often higher than the appraised value because the timber will be cut later and the buyers are anticipating future rather than present markets. With the available supply of timber eligible for logging remaining relatively stable each year based on public policy, the price will rise as the market demand rises. For example, in 1979 when the construction industry was in a boom, the price of sawtimber was $173 per 1000 board feet. By 1982 -- when the construction industry slumped -- the price had fallen to $61.

Impact of Duties on Housing Consumers

The removal right provision of proposed legislation could substantially increase the price of timber if subsidy is redefined as proposed in H.R. 2451 and S. 1292.

Lumber is the main building material used in home construction and housing construction currently accounts for over 60% of the softwood lumber consumed in the United States. The Census Bureau estimates that the average annual value of new residential construction from 1964 - 1984 (in constant 1977 dollars) was $67.68 billion. According to the Bureau of Labor Statistics, single-family construction worth $1 billion creates 22,000 jobs. Of those, 9,500 are in the construction and land development industries and 12,500 are in manufacturing, mining, transportation, wholesale trade, services and other industries.

Lumber is a key part of home construction. In 1984, lumber was 22% of total hard construction costs. From the average priced house in 1985 of $100,700, lumber cost $8,545 - roughly 9% of the final price to the consumer. If the domestic price of lumber had increased during that period by 30%, which our economics department estimates to be a likely increase based on a 60% duty on Canadian lumber, the average priced home would have been $2,555 higher. If the duty were more modest, it could raise housing costs by as much as $1,000. NAHB estimates that for every $1,000 increase in the price of an average home, more than 300,000 families are priced out of the housing market. As home buyer demand decreases, fewer houses are built, and the industry begins laying off workers. This is a cycle with which we are all too familiar.

Conclusion

In conclusion, NAHB would like to thank the Committee for the opportunity to present our views for the record on bilateral negotiations between the United States and Canada on a comprehensive free trade arrangement. NAHB supports a free trade agreement between the two countries including unrestricted trade on Canadian softwood lumber imports.

TESTIMONY OF THE NATIONAL ASSOCIATION OF MANUFACTURERS

BY

LAWRENCE A. FOX

ON

U.S.-CANADA TRADE NEGOTIATIONS

BEFORE THE COMMITTEE ON FINANCE

OF THE UNITED STATES SENATE

APRIL 11, 1986

Mr. Chairman, Members of the Committee, I am Lawrence A. Fox, Vice President for International Economic Affairs of the National Association of Manufacturers. We understand, Mr. Chairman that one option open to the Finance Committee on the question of the prospective bilateral trade negotiations with Canada was to do nothing. That is the Book-of-the-Month Club option: Don't do a thing. The book and the bill will come in due course. The issue of a new trade agreement with Canada is too important for that, Mr. Chairman. NAM commends you for calling these hearings, and we are grateful for the opportunity to express our views on this issue.

The National Association of Manufacturers, founded in 1895, is the oldest national trade association. At present, we have over 13,000 members, and collectively they represent about 80 percent of U.S. industrial output. Their employees make up roughly 85 percent of U.S. industrial employment.

My purpose today is to discuss U.S.-Canada trade, not the larger issue of U.S. trade and competitiveness. I would note, however, that in 1985 the U.S. deficit in manufactured goods alone, $114 billion, was equal to 76 percent of the total trade deficit of almost $150 billion. Manufactures account for 71 percent of U.S. imports, for 68 percent of our exports globally, and for about 85 percent of our exports to Canada. The stake of American industry in any trade negotiation, therefore, is enormous.

NAM RESOLUTION

I have included as part of my statement the NAM Resolution on U.S.-Canada Trade, which was approved unanimously by our board of directors in February. This states that, "The National Association of Manufacturers supports the proposal for U.S.-Canadian bilateral trade negotiations," and through it the NAM "urges the Administration and the Congress to move forward toward a new framework for the U.S.-Canadian economic relationship." It gives our reasons for believing that there are advantages to be gained for U.S. industry, and it expresses some of our caveats and concerns.

An economic consultant in Ottawa has dubbed the proposed free-trade-area talks the BETA negotiations, for Bilateral

ADOPTED BY NAM BOARD OF DIRECTORS
FEBRUARY 7, 1986

NAM STATEMENT ON U.S.-CANADA TRADE

The National Association of Manufacturers appreciates that American economic relations with Canada are different in several important respects from our economic relations with other countries. Canada is America's largest foreign customer, our principal foreign supplier, and the recipient of more U.S. investment than any other country. Because it is spread across a continent, U.S.-Canadian trade is as much a series of regional phenomena as it is a relationship between two separate nations.

The very closeness of our economic cooperation has created a situation in which government interference with the markets of the two countries can be a greater cause for concern for both American and Canadian businesses than in other economic relationships.

For these reasons and because of the potential for building on the existing high level of business cooperation between our two countries, the National Association of Manufacturers supports the proposal for U.S.-Canadian bilateral trade negotiations.

Any agreement resulting from these negotiations should advance the economic interests of American industry. The opportunities to do so are numerous. They include tariff reductions, meaningful reductions in Canadian federal and provincial subsidies, reductions in Canadian federal and provincial non-tariff barriers, enhanced protection for intellectual property rights, and agreed limits over the Canadian government's ability to restrict and/or control U.S. investment in Canada. In addition, an effective and expedited disputes settlement procedure should be obtained, as well as an agreed procedure for consultations regarding the exchange rate between the Canadian and U.S. dollar so that trade distortions arising from this cause can be resolved. The NAM believes that success in these areas is likely only if the U.S. Government accords significant weight to the advice it receives from the U.S. private sector in the course of the negotiations. If these goals are not substantially achieved, NAM will not be able to support a new trade agreement with Canada.

Because of the importance of securing an agreement that advances U.S. economic interests, the U.S. Trade Representative should include as part of the Administration's explanation of the agreement a clear statement of the agreement's expected economic impact on U.S. interests when the time comes for an agreement to be submitted to the Congress.

NAM believes that the resolution of existing disputes between the United States and Canada should be given a high priority. The sooner these matters can be cleared from the U.S.-Canadian agenda of commercial issues, the greater the likelihood that a trade enhancement agreement benefical to both countries can be negotiated.

In the hope that such an accord can be achieved, the National Association of Manufacturers urges the Administration and the Congress to move forward toward a new framework for the U.S.-Canadian economic relationship.

-NAM-

Enhanced-Trade Agreement. By whatever name, the impetus for these negotiations seems to derive from two quite different strains in Canadian thinking. On the one hand, Canada seeks to assure her producers of even more secure access to the U.S. market. On the other, government officials and others in Canada believe that the discipline of more open trade with the United States will help foster a family of more competitive Canadian industries. Put in terms of simple metaphores, Canadians want to give their exporting industries the warm milk of secure access, and they want to administer a cold, sobering but invigorating, shower to the Canadian industrial economy as a whole.

Our response to the proposal for free-trade-area negotiations can draw from these ideas, but it has to begin with this question: Why is it that the United States has a $22 billion trade deficit with a country that is, in many respects, less competitive?

National economies are complex phenomena, and there are a number of reasons for this anomaly. Certainly one reason is the current web of Canadian protectionism. The U.S. furniture industry presents an excellent illustration of this problem, and it is unfortunately only one of many. Illinois printers who face discriminatory postal rates in Canada and a tariff of over 30 percent on catalogues to Canada offer another; Alabama producers of insect screening another; and U.S. brewers and wine makers another. Dismantling that protectionism should be a boon to both the U.S. and Canadian economies. It will help redirect Canadian resources to their most productive industries, and it ought to give U.S. producers a better chance to reap the export earnings that their productivity should have earned them. Additionally, it should enable companies with facilities on both sides of the U.S.-Canadian border to rationalize their production facilities. That too can only be in the interest of both the United States and Canada.

But what of Canada's desire to enhance her security of access to the U.S. market? NAM agrees with the general position expressed by U.S. Administration officials that everything should be on the table. At the same time, we think it is important not to be confused by Canadian rhetoric. Their officials complain about our contingency protection. As Table 1 below illustrates Canada's trade surplus with the United States has been increasing steadily at least since 1977, and it is now second only to our deficit with Japan. That is hardly evidence of protectionism.

Further, when we examine the phrase "contingency protection", we find that the "contingencies" in question are generally unfair trading practices that hurt U.S. industries and the "protection" is the use of GATT sanctioned responses to those practices. Of course we should talk about these issues. In the context of a wholly new arrangement for U.S.-Canada trade, it may be that changes in their laws and ours will make sense that do not make

TABLE 1

U.S. TRADE WITH CANADA 1977-1985

	Exports	Imports	Balance
1977	25.0	30.6	- 5.6
1978	27.6	34.6	- 7.0
1979	32.2	39.0	- 6.9
1980	35.4	42.0	- 6.6
1981	39.6	46.8	- 7.6
1982	33.7	46.8	-13.1
1983	38.2	52.5	-14.3
1984	46.5	66.5	-20.0
1985	47.3	69.4	-22.1

Source: U.S. Department of Commerce, Highlights of U.S. Export and Import Trade, 1977-1983. Imports c.i.f.

sense when considered in isolation. Nevertheless, Canada should not pin her hopes or her negotiating strategy on revolutionizing or undermining the U.S. unfair trade statutes.

OUTSTANDING ISSUES

As stated in our resolution:

> NAM believes that the resolution of existing disputes between the United States and Canada should be given a high priority. The sooner these matters can be cleared from the U.S.-Canada agenda of commercial issues, the greater the likelihood that a trade enhancement agreement beneficial to both parties can be negotiated.

It is not necessary to rehearse these issues. Both sides know what they are, and it is not our belief that general negotiations should be held hostage to any one issue.

Yet there is one, I think, that has become especially important. This is the pharmaceutical issue. From the U.S. perspective, it embodies high economic stakes, an important commercial principle. and the ability of each partner to rely on the good faith of the other.

Canada is not the only country in the world in which the bulk of medical costs are borne by the public sector. Indeed, the United States is probably the only major industrial country where this is not the case. Yet Canada is alone among industrial countries in its policy of using compulsory licensing of new drugs as a way of controlling medical costs. This seems to us a bad policy for Canada, as it effectively discourages anyone who might otherwise invest in pharmaceutical research and development in Canada.

Compulsory licensing is certainly a bad principle as far as the NAM is concerned. We believe that the future of open international trade depends upon building strong protections for intellectual property rights into the international trading system. Compulsory licensing flies in the face of that effort. Finally, this issue is critical because it touches on issues of trust. The U.S. government has received repeated assurances that Canada's present compulsory licensing law, Section 41 of the Canadian patent law, would be amended. It hasn't happened yet. If the Canadian government's promise to modify their compulsory licensing program is not quickly redeemed, the issue could cast a cloud over the proposed bilateral trade negotiations and dim chances for success in this effort.

NEGOTIATIONS

As to the issues which are widely expected to be part of the negotiations, it is perhaps too early to set out precise objectives. There is still a great deal to be learned. Most of the broad areas for negotiation have been identified by one side or the other, and we do not need to dwell on them at this time. There are three, however, which need to be emphasized more than they have been.

Investment. The first is investment. It is odd to us that the Canadian Trade Negotiations Office (TNO), which has been set up under Simon Riesman to handle these negotiations, has teams working on tariffs, trade in services, government procurement, and other topics, but none on investment. This is not an oversight. We have heard Canadian officials argue that there is no need for investment issues to be included in these negotiations. They are wrong. And the National Association of Manufacturers would strongly oppose any trade agreement with Canada that did not include meaningful investment provisions.

It is ironic that Canada should object to including investment in light of the important role investment policy has already played in bringing us to this juncture. The United States and Canada are not only each other's largest trading partner; each is the other's largest investment partner as well. U.S. investment in Canada is about $90 billion and Canadian investment in the United States is about $30 billion. Yet, as you know, Mr. Chairman, Canadian investment policies, specifically the policies of the now defunct Foreign Investment Review Agency, have been among the most contentious issues in recent years between the United States and Canada. Many of these policies have been trade distorting, and some have been found to be in violation of the GATT. Canada's well publicized movement away from the policies and attitudes of FIRA -- its establishment and promotion of the FIRA replacement Investment Canada -- are among the developments that have given credibility to the idea of a free-trade-area.

It would be foolish for the United States to enter a major agreement with Canada without incorporating into that agreement the investment conditions that make it possible. In saying this, I am not necessarily expressing the view that the move from FIRA to Investment Canada has by itself created those conditions, but certainly it has been a step in the right direction.

A further irony in Canada's reluctance to discuss investment policies in the context of the trade talks is that she is clearly selling investment in Canada on the basis of Canada's good trading relationship with the United States and the prospect of an even better one. Investment Canada has offices in New York, Chicago, Los Angeles, London, Paris, Bonn and Tokyo, and their message is this. Put your North American plant in Canada and reap the advantages of a market of 250 million people. We have no quarrel with that, but the investment must be free and unrestrained.

Exchange Rates. Another difficult issue that should form part of a trade agreement between the United States and Canada is the question of the exchange rate between the U.S. and Canadian dollars. If we have learned anything in the last five years it is that serious misalignments in exchange rates can make a mockery of the best trading arrangement. It should be obvious that a free-trade-area accord with Canada should include, as a matter of course, a consultation mechanism for dealing with potential problems in the exchange rate relationship between the two dollars.

Dispute Settlement. Canadian official frequently express the view that there would have to be an international, U.S.-Canada dispute settlement body establishment to make a major new agreement work. We agree. We favor a bilateral dispute settlement procedure which will solve problems rather than perpetuate disputes--possibly by means of a standing joint commission.

CONCLUSION

A lot is made of the disparity in size between the United States and Canada and the fact that these negotiations loom larger in Canadian politics today than they do in our own. There is the impression that this is an enormously important question for Canada but just a ho-hum issue for the United States.

That impression may serve Canadian negotiators, but it could not be more inaccurate. Our 1985, $150 billion trade deficit is the inescapable evidence that there is a crisis in American trade and American competitiveness. Our country cannot afford any more big mistakes in trade. We cannot afford to miss an opportunity to increase our exports or to make our factories more efficient and more competitive. And we cannot afford a trade deal with our largest trading partner that does not advance the interests of U.S. industry.

NAM's hope, Mr. Chairman, is that this Committee will approve the Administration's plan to enter into bilateral negotiations with Canada. We believe an affirmative statement to this effect is desirable. We are sensitive to the fact that the requirements of the negotiating process itself impose limits on any such statement. To anticipate the compromises that one expects would undercut our negotiators, while too rigid a statement of Congressional requirements might preclude the compromises that will be essential to a good agreement. What the Committee can and should do, we believe, is to reinforce the position that a trade agreement with Canada must advance the economic interest of U.S. industry or it will not be approved.

I said at the outset, Mr. Chairman, that we regard this as an important hearing. More important still, of course, will be the hearing I hope you will be able to call in 18 months, or two years, when the question will be: How should Congress vote on the new trade agreement with Canada. We would like to testify at that hearing too. I hope we will be testifying in favor of the agreement, but that will depend on the agreement itself.

Thank you.

NATIONAL ASSOCIATION OF RECYCLING INDUSTRIES, INC.
330 MADISON AVENUE / NEW YORK, N.Y. 10017 / (AREA CODE 212) 867-7330

BEFORE THE
COMMITTEE ON FINANCE
UNITED STATES SENATE
WASHINGTON, D.C.

Proposed U.S.-Canada
Free Trade Negotiations

STATEMENT OF
NATIONAL ASSOCIATION OF RECYCLING INDUSTRIES, INC.

This statement is submitted by the National Association of Recycling Industries, Inc. (NARI) in response to the Committee's Press Release No. 86-022 of March 26, 1986 which solicited comments regarding the broad implications of possible negotiation of a comprehensive free trade arrangement between the United States and Canada.

Essentially, NARI favors the negotiation of a free trade agreement between the United States and its good neighbor to the north, and urges the Finance Committee to approve and support the commencement of such negotiations under Section 102 of the Trade Act of 1974, as amended by Section 401 of the Trade and Tariff Act of 1984.

Introduction

NARI is the trade association for the nation's metals, paper and textile recycling industries. Its membership consists of approximately 1,000 firms located throughout the United States, all of which are engaged in various commercial aspects of the recovery, brokering, processing, domestic industrial utilization of —or foreign trade in— the aforesaid recyclable materials.

NARI's membership encompasses all segments of the recycling industry. It includes scrap processors with extensive plant facilities for the handling of large volumes of industrial and post-consumer waste materials. These processors segregate and prepare many types of recycled metals and other recycled materials for eventual market consumption by a wide variety of mills and manufacturing industries here in the United States and abroad.

The industrial user segment of NARI's membership consists of refineries and smelters that convert recycled aluminum and metal scrap into ingots and alloys for castings and other fabricated products; brass mills and steel mills; smelters of lead and zinc; paper mills and paperboard manufacturers, and dozens of other industries that regularly use recycled materials in their manufacturing operations.

Finally, NARI's membership includes other companies which engage in extensive international trade activities in various recycled materials, principally metals and paper. These exporters ship surplus tonnages of those recycled commodities in foreign commerce to America's trading partners throughout the world.

Statistics demonstrate, therefore, that each year the U.S. recycling industry supplies both the United States and many of its foreign allies, including Canada, with significant portions of their total raw material needs. In 1985, for example, over 45% of this nation's copper raw material supply was derived from recycling, along with almost half its lead, 35% of its aluminum, 30% of its iron and steel, practically 20%

of its zinc and about 20% of its paper and paperboard supplies. In the foreign trade sector, the exportation of recycled materials substantially helped the U.S.' balance of payments position, and materially expanded international business opportunities for American exporters.

Concomitantly, the broad industrial use of recycled raw materials here at home has served to (a) conserve energy and scarce domestic depletable virgin resources, (b) reduce the United States' reliance on foreign imports of critical virgin raw materials, and (c) aid cities and states across the country in the costly struggle against growing solid waste disposal problems and costs.

NARI Favors The Establishment And Expansion Of Free Trade Arrangements With Canada, Especially With Reference To Trade In Recycled Materials Such As Scrap Metals And Paper.

As indicated above, NARI and its members vigorously support the negotiation and maintenance of free trade arrangements between the United States and Canada. NARI thus urges the Committee to approve and support the President's proposal to negotiate a comprehensive bilateral free trade agreement with that country, as apparently proposed by Prime Minister Mulroney last September.

More specifically, NARI submits the negotiations should provide for free, open, unrestricted and unimpeded trade in recycled metals and paper between these two neighboring nations of North America. Trade in recyclables between the two countries should not be subjected to duty or other economic restrictions that operate to limit the channels of trade and commerce. Absent emergency conditions normally non-existent, scrap iron and steel, recycled nonferrous metals and recycled paper should move across the common borders of the United States and Canada unhindered, and without any kind of restrictive impediments or regulations. To restrict such trade is clearly not in the interest of the United States for the following reasons:

1. Generally, more recycled materials are shipped from the United States to Canada than from Canada to the U.S. For example, average annual scrap iron and steel shipments to Canada for the period 1983 to 1985 were estimated to have been 560,000 short tons, while the average annual imports from Canada were estimated to have been 535,000 short tons for the same period.

2. The types of scrap metal moving into the U.S. from Canada are needed by U.S. consumers.

3. Import duties on scrap iron and steel, for example, have been suspended for over a decade without any injury to or adverse impact on either the U.S. economy, U.S. industry or U.S. labor.

4. The imposition of import duties on iron and steel scrap from Canada would result in higher prices for the imported material at a time when the United States is seeking to restrain inflationary pressures.

5. Our relations with Canada have been those of a most friendly neighboring country, and a free trade arrangement would be a positive and constructive act on the part of the two governments aimed at improving that relationship. The domestic recycling industry's commercial activities are closely intertwined with those of Canada's, and therefore the establishment and expansion of free trade relationships between the two nations is crucial to the maintenance and growth of these business ties which plainly have an important salutary impact on the national interests of both countries.

In The Course Of Negotiating A Free Trade Agreement With Canada, The United States Should Strive To Eliminate Non-Tariff Barriers In The Form Of Conflicting And Non-Uniform Environmental Import-Export Requirements And Regulations.

In the absence of a bilateral trade agreement, Canada and the United States are unfortunately in the process of establishing non-tariff trade barriers in the form of conflicting, diverse environmental import-export regulations and requirements that operate effectively to reduce or restrict trade in important recycled raw materials, principally metals. In order to maximize free trade in these important commodities, it is essential for U.S. and Canadian negotiators to agree from the very outset that recycling *per se* is crucially important and beneficial to the environment, and thus no environmentally-inspired impediments to free trade should be imposed on clearly non-hazardous recycled metals. In this regard, of course, the U.S. Environmental Protection Agency has exempted scrap metals from its hazardous waste regulations under the Resource Conservation and Recovery Act, as amended, and both houses of Congress have recently exempted recycled metals from Superfund hazardous waste taxation.

Canada, however, has its own regulatory regimes which it enforces, so clearly if free trade negotiations proceed, steps must be taken to establish uniform rules and regulations which will not limit or prevent trade relations in recycled metals between the two nations.

Conclusion

The Senate Finance Committee should approve and support the President's request to negotiate a free trade arrangement with Canada, and such negotiations should clearly encompass the establishment of free trade in recycled materials and the elimination of conflicting, diverse environmental non-tariff barriers which automatically reduce or foreclose free, open trade between the two nations.

Respectfully Submitted,

Edward L. Merrigan, Counsel
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April 24, 1986

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COMMITTEE ON INTERNATIONAL TRADE AND TRANSACTIONS

LAUREN D. RACHLIN
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New York State Bar Association®

TO: Senator Bob Packwood, Chairman and Members of the Senate Finance Committee

RE: U.S. - Canada Trade Negotiations

The New York State Bar Association Committee on International Trade and Transactions supports the proposed bilateral trade negotiations between the United States and Canada.

A bilateral free trade area of Canada and the U.S. would have several important advantages for both sides. Canadian exports pose little structural danger to U.S. jobs, unlike exports from the newly industrializing and low-wage countries of the third world. At the same time, free access to U.S. markets is vital for Canada, which directs fully 70% of its exports to the U.S.

Several advantages for the U.S., too, would be forthcoming from freer trade with Canada. These include assuring the beneficial treatment of the large U.S. direct investment position in Canada, and the improvement of ties with a neighboring society with which we have a unique economic and political affinity.

Protectionist pressures arising from the very large U.S. trade deficit, however, could impede progress in this area. The most dangerous possibility is the imposition by the U.S. of a GATT-sanctioned quota to protect some specific U.S. industry, that inadvertently disrupts trade with Canada.

NYSBA

Several barriers to trade between Canada and the U.S. remain, despite the generally open trade between our two countries. Diminishing them through comprehensive bilateral trade liberalization would probably be the most effective way to push us along the route to closer trade ties. This would have the additional benefit of providing some concrete progress in sustaining the process of international trade liberalization while we wait for the results of the latest GATT round.

The chief alternative to an across the board approach--market-by-market liberalization--seems relatively unattractive. It is admittedly the case that the bilateral automobile free trade agreement has been an enormous success, but finding another single sector or even a combination of sectors that offers similar, predictable, balanced gains to both sides may be so tedious as threaten to outweigh the possible gains.

Respectfully yours,

Lauren D. Rachlin

WRITTEN STATEMENT ON BEHALF OF THE OUTDOOR POWER EQUIPMENT INSTITUTE, INC. SUBMITTED TO THE COMMITTEE ON FINANCE U.S. SENATE

I. INTRODUCTION

This statement is submitted on behalf of the Outdoor Power Equipment Institute, Inc. ("OPEI"), a nonprofit trade association representing manufacturers of outdoor power equipment and suppliers to the industry. The statement is submitted in support of the establishment of a comprehensive free trade arrangement with Canada. 1/ Establishment of such an arrangement would confer substantial benefits on U.S. manufacturers of outdoor power equipment and the components used in their manufacture.

The U.S. outdoor power equipment industry has aggressively pursued the Canadian market for many years. Notwithstanding these efforts, however, U.S. exporters have met with consistently high tariff barriers that have substantially eroded the competitive advantages previously enjoyed by the U.S. industry. These tariff barriers are particularly unreasonable when compared with the tariff rates on comparable products imported into the United States. Establishment of a comprehensive free trade arrangement with Canada in which outdoor power equipment were included would ensure reciprocity in this sector, where none currently exists.

Additionally, the U.S. industry, in attempting to export to Canada, has noted increasing indications of a government-backed protective policy. This policy is reflected in the efforts of Canada's Department of National Revenue for Customs and Excise ("Canadian Customs") to reclassify imports of certain U.S. outdoor power equipment products into higher-dutied categories. This policy has led certain U.S. manufacturers to

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1/ Notice of the Committee's request for written comments on the establishment of a free trade arrangement with Canada was published in Committee on Finance Press Release #86-022, dated March 26, 1986.

reconsider their practice of exporting to Canada, and in some instances, to consider moving assembly facilities into Canada to circumvent this trade barrier. A free trade arrangement would negate the adverse impact of this protective policy and discourage U.S. firms from exporting jobs through the establishment of production facilities abroad.

OPEI firmly believes that the establishment of a comprehensive free trade arrangement would provide substantial benefits to U.S. manufacturers of outdoor power equipment who have traditionally exported such products to Canada. Furthermore, establishment of such an arrangement would benefit Canadian manufacturers of outdoor power equipment who import from the United States virtually all of the gasoline-powered engines used in the manufacture of such Canadian products, as well as other significant components.

While the Canadian outdoor power equipment industry is in the process of development, the Canadian market for most outdoor power equipment remains largely dependent on the United States. Accordingly, the benefits of a free trade arrangement would be shared not only by U.S. and Canadian manufacturers, but by Canadian consumers as well.

For these reasons, OPEI supports the establishment of a comprehensive free trade arrangement with Canada and respectfully requests that the Committee on Finance provide the necessary support and authorization for the upcoming negotiations. Further, OPEI requests that if these negotiations are to proceed on a sectoral basis, as was originally contemplated, the Committee should support inclusion of outdoor power equipment in the negotiations.

II. PARTY IN INTEREST

OPEI is a national trade association, composed of lawn-and-garden equipment manufacturers. Founded in 1952, OPEI advances the economic interests of its members and the general welfare of the U.S. industry.

OPEI membership is composed of two classes — regular and associate. Regular members include any individual or firm engaged in the domestic manufacture, fabrication or assembly of the following equipment intended primarily for consumer use: walk-behind mowers, walk-behind rotary snow throwers, walk-behind rotary tillers, lawn tractors and riding mowers, garden tractors, flexible line trimmers, edger/trimmers, shredder/grinders, leaf blowers, lawn vacuums, lawn sweepers, sprayers, power rakes and thatchers, chippers, stump cutters, log splitters and commercial turf care equipment. Associate members are those who manufacture the following components and attachments for the products listed above: power source (engines), brake assemblies, clutch assemblies, transmissions, oil filters and spark plugs, decks, belts, tires, mufflers, controls, seats, blades, grass catchers, mower, tillage and snowthrower attachments, batteries and financial services. A list of OPEI members is attached hereto as Appendix A.

The companies represented by OPEI are extensively involved in the production of outdoor power equipment and their components. Many of these companies have exported these products to Canada. Accordingly, these companies would benefit from the establishment of a comprehensive free trade arrangement with Canada and have a direct interest in the inclusion of these products in such an arrangement.

III. THE BENEFIT TO U.S. OUTDOOR POWER EQUIPMENT MANUFACTURERS OF A FREE TRADE ARRANGEMENT: ELIMINATION OF UNFAIR CANADIAN TARIFFS

A. U.S. Exports to Canada Have Been Adversely Affected by Inordinately High Canadian Tariffs

The U.S. outdoor power equipment industry has been traditionally export-oriented. While the level of exports has varied considerably, in most instances, U.S. manufacturers have exported anywhere from five to 10 percent of their total shipments. 2/ The largest single-market for U.S.-produced lawn-and-garden equipment has been, and continues, to be, Canada.

Between 1980 and 1983, total exports of U.S. outdoor power equipment to Canada dropped from $91.1 million to $57.7 million, a decline of almost 30 percent (see Table 1). This downward trend was halted in 1984 due in large part to significant increases in exports of gasoline engines to Canadian manufacturers. Nevertheless, in 1985, total exports of U.S. outdoor power equipment to Canada dropped almost 20 percent, from $83.9 million in 1984 to $67.3 million in 1985. Declines were registered in virtually all product categories. While these declines are reflective of world-wide trends in the export of U.S. outdoor power equipment, the factors underlying decreasing shipments to Canada are unique since the Canadian dollar has not experienced the same degree of depreciation against the U.S. dollar as other foreign currencies. 3/ Indeed, between 1980 and 1985, the Canadian dollar has depreciated only 16.8 percent against the U.S. dollar. Such depreciation cannot therefore be held accountable for the overall decline in U.S. exports to Canada.

2/ U.S. Department of Commerce, 1984 U.S. Industrial Outlook (1984) at 44-19.

3/ The 16.8 percent depreciation of the Canadian dollar against the U.S. dollar over the 1980-1985 period is relatively insignificant when compared with the rate of depreciation against the dollar of other foreign currencies in countries where the market for U.S. outdoor power equipment has been strong. For example, in France, the franc has depreciated 36.5 percent against the U.S. dollar; in Great Britain, the pound has depreciated 79.1 percent; and in Germany, the mark has depreciated 61.9 percent.

OPEI believes that the drop in U.S. exports of outdoor power equipment to Canada results from persistently high Canadian tariffs, and more recently, from the Canadian Government's policy of enhancing the impact of its already high tariffs by reclassifying imports of certain U.S. outdoor power equipment into higher-dutied categories. Accordingly, the ability of U.S. producers to compete in the Canadian market has been substantially undercut.

B. Canadian Tariffs on Imports of Lawn-and-Garden Products Exceed Those Imposed on Imports of Comparable Products into the United States

In an effort to protect a small but growing manufacturing industry, the Canadian Government has imposed a series of high tariffs on certain imports of lawn-and-garden equipment. These tariffs are substantially higher than the tariffs imposed by the United States on comparable products (see Table 2). Indeed, with respect to lawn mowers, Canadian tariffs are currently 131 percent higher than the duty on comparable U.S. products; with respect to lawn mower parts, 50 percent higher; with respect to snow blowers, 98 percent higher; and with respect to engines, 1,400 percent higher.

Only with respect to tractors is there comparability, in that both countries permit entry of these products duty free. Even in this product area, however, where reciprocity should exist on the basis of the relevant tariff statutes, the interpretive policy of Canadian Government officials has virtually eliminated the prospects for equal treatment.

The wide disparity in the relative duty rates on comparable U.S. and Canadian products, and the unfair competitive advantage these disparate duty rates confer on a limited number of Canadian manufacturers, provide compelling support for a comprehensive free trade arrangement that would include this manufacturing sector. Indeed, it is the recent application of these duty rates by the Canadian Government, however, which has proven to be the biggest obstacle to the U.S. industry, and which has primarily motivated OPEI to submit this statement to the Committee.

C. The Canadian Government is Limiting U.S. Exports of Outdoor Power Equipment Through a Policy of Reclassifying Certain Items into Higher-Dutied Categories

Prior to 1982, the basic tractor (or power unit) of certain outdoor power equipment was separately classified under tariff item 40938-1 — a duty-free category. Various interchangeable attachments that may have accompanied the tractor unit were classified according to established guidelines under dutiable tariff items such as 42505-1 (lawn mowers) and 42761-1 (machines and tools, including blades, loaders, rippers and related operating and controlling gears).

In 1981, the Canadian Tariff Board issued a ruling that resulted in the reclassification of imports of two-wheeled walk-behind tractors with snow blower attchments from the *duty-free* tariff category 40938-1 for the tractor, and the dutiable category 42761-1 for the snow blower attachment, to tariff item 42700-1, "machines, not otherwise provided for," — which carries a 10.7 percent duty on the *entire* product. As a result of the ruling, U.S. snow blowers, the tractor portions of which were previously imported into Canada duty free, are currently subject to a 9.9 percent duty. 4/

Although the decision covered only two-wheeled walk-behind tractors with snow blower attachments, Canadian Customs officials have applied the policy reflected in the Tariff Board decision to imports of most tractor-based units. Thus, for example, most lawn-and-garden tractors, which were previously subject to duty-free treatment under Canadian tariff item No. 40938-1, are now classified under the specific provision for "power lawn mowers" in tariff item No. 42505-1, on the basis that these tractor units

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4/ The rate of duty will be reduced to 9.2 percent by 1987.

are exported in conjunction with mower decks. This tariff classification requires the payment of a duty of 11.1 percent on the entire value of the item. 5/

The application of this policy to most lawn-and-garden tractors is currently the subject of a proceeding now pending before the Canadian Tariff Board (Appeal No. 2294). At issue in that proceeding is the classification of lawn-and-garden tractors manufactured in the United States, and specifically the criteria to be used by Canadian Customs in rendering such classification decisions.

Notwithstanding the pendency of this proceeding, Canadian Customs officials have applied the policy underlying the 1981 Tariff Board decision to most U.S.-manufactured lawn-and-garden tractors, reclassifying the previously duty-free items into a higher-dutied "power lawn mower" category. The impact of this policy is reflected in the sharp decline in U.S. exports of lawn-and-garden tractors to Canada (see Table 1). Since exports of these products comprise more than 25 percent of total U.S. sales of outdoor power equipment to Canada, the steep decrease in such exports must be viewed as a major factor in explaining the overall decline in U.S. exports to Canada between 1982 and 1985. If the Canadian Tariff Board sustains these classification practices, the ability of a large segment of the U.S. outdoor power equipment industry to compete in the Canadian market will be threatened. A U.S.-Canada free trade arrangement would eliminate this concern.

IV. CANADIAN MANUFACTURERS AND CONSUMERS OF OUTDOOR POWER EQUIPMENT WILL BENEFIT FROM A FREE TRADE ARRANGEMENT

As previously discussed, U.S. exporters of outdoor power equipment would benefit from the elimination of the unreasonably high tariffs and restrictive classification policies that have undercut the once strong market position of the U.S. outdoor power equipment industry in Canada through the establishment of a

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5/ The rate of duty will be reduced to 10.2 percent by 1987.

comprehensive free trade arrangement. The beneficiaries of this program, however, would not be limited to U.S. manufacturers. Indeed, OPEI believes that Canadian manufacturers of outdoor power equipment, as well as Canadian consumers, will benefit if a free trade arrangement were established.

First, Canadian manufacturers rely almost exclusively on U.S. manufacturers of gasoline-powered engines in the production of most outdoor power eqiupment. As is evidenced in Table 1, U.S. exports of gasoline-engines have grown considerably since 1982, reflecting the growing demand of a developing Canadian industry. If the duty on engines currently maintained by the Canadian Government were eliminated, Canadian manufacturers would benefit from a 7.5 percent reduction in the cost of the most complex and expensive component used in the manufacture of their products.

Canadian consumers would benefit as well. For example, a $7.50 saving on the cost of a $100 U.S.-made engine, which may comprise more than 50 percent of the total manufacturing cost of a walk-behind lawn mower, could result in a savings for the consumer at retail of almost $20.00, or more than five percent of the retail price. Given the fact that price is the principal factor motivating consumer selection in this sector, the five percent consumer savings resulting from the elimination of the duty on imported engines could enhance the overall health of this increasingly important Canadian industry, and would stimulate the growth of the economy as a whole, as a result of the substantial savings passed on to the consumer.

In sum, elimination of the protective tariffs on such price elastic consumer products as lawn mowers and snow blowers, as well as on the engines contained in those products, would afford Canadian consumers a wider selection of products — both Canadian and American — at significantly lower prices. The beneficiaries of these opportunities would include homeowners, small farmers, commercial property owners, and the entire lawn-and-garden care industry of Canada.

V. CONCLUSION

OPEI believes that a comprehensive U.S.-Canada free trade arrangement will result in mutual benefits to manufacturers in both countries. In the case of the U.S. outdoor power equipment industry, it will provide an opportunity for U.S. manufacturers to compete in a growing export market, unfettered by unreasonable tariff barriers, and permit the U.S. industry to translate its competitive advantages into real commercial gains. In the case of the comparable Canadian industry, the arrangement will provide Canadian manufacturers with the opportunity to purchase components from U.S. firms at substantially reduced costs, thereby decreasing their costs of production. Finally, a U.S.-Canada free trade arrangement will afford Canadian consumers — both commercial and residential — a wider selection of quality products at lower prices. For these reasons, the Outdoor Power Equipment Institute, Inc. supports the establishment of a U.S.-Canada free trade arrangement and urges that such an arrangement include outdoor power equipment and the various components that go into the production of such equipment.

Hearing Date: April 11, 1986

COMMENTS OF
THE RICE MILLERS' ASSOCIATION
CONCERNING THE PROPOSED NEGOTIATION OF
THE U.S.-CANADA FREE TRADE AGREEMENT

Submitted to
Committee on Finance
U.S. Senate

April 4, 1986

INTRODUCTION

In response to the request for public comments, these comments on the proposed negotiation of the U.S.-Canada free trade agreement are filed by The Rice Millers' Association, a national trade association for the U.S. rice industry. RMA's members consist of farmer-owned cooperatives and independently owned rice milling companies located in Arkansas, California, Louisiana, Mississippi, and Texas. (A list of the members of RMA is attached.) The farmer-owned cooperatives belonging to RMA grow approximately 55 percent of the rough rice produced in the United States and include over 12,000 rice farmers. In addition, the independent rice milling companies that are RMA members, together with the farmer-owned cooperatives, account for virtually all of the rice milled in the United States. In short, RMA members grow, mill, and market the majority of the rice sold domestically, as well as abroad.

The Rice Millers' Association supports in principle the establishment of a free trade arrangement between the United States and Canada. If agricultural commodities and products are covered by the agreement ultimately negotiated, rice and rice products should receive the same favorable duty treatment as other products and commodities. The Association submits that free trade in rice and rice products between the United States and Canada will promote the national interest.

BACKGROUND

In 1985, the United States exported 101,279 metric tons of rice to Canada, with a value of U.S. $41,290,425.00. (The figures for 1984 are comparable.) The United States is the largest supplier of rice to the Canadian market, but is beginning to face increased competition from Thailand. Thai rice exports are increasing because of the price advantage Thai producers enjoy. The only other significant competition comes from India.

There is no domestic rice production in Canada. The Canadians grow wild rice, but otherwise are dependent on foreign suppliers. The duties applied to rice and rice product imports raise consumer prices and thus put a dampening effect on consumer demand. Such tariffs are unnecessary to protect a domestic industry.

The bulk of U.S. exports to Canada are subject to duties. Although rice in the husk (paddy or rough) and husked (brown) rice enter duty free, total U.S. exports of these types of rice in 1985 accounted for only 875 metric tons. Semi-milled or wholly milled rice and broken rice are dutied at the rate of $5.51 per ton. U.S. exports (excluding 183 metric tons donated for relief or charity) in 1985 totalled 100,221 metric tons. Additionally, U.S. companies continue to export prepared rice products to Canada, for which duties range from 7.5 percent *ad valorem* to 10 percent *ad valorem* depending upon the size of the package. We estimate that Canadian importers paid approximately Can. $600,000 in duties in 1985 on rice and rice product imports from the United States.

BENEFITS OF A FREE TRADE ARRANGEMENT

The Rice Millers' Association has long supported free trade. The $2 billion U.S. rice industry is particularly export dependent. Approximately two in every three acres of rice is grown for export. As a result of successive world record rice crops, the strength of the U.S. dollar, and the high price support level (relative to world prices) mandated by U.S. farm legislation, U.S farmers have steadily lost a significant percentage of their world market share. Canada remains a particularly attractive export market. The 1985 Farm Bill was designed to encourage exports of rice. The proposed negotiation of a free trade agreement with Canada complements that effort by further promoting exports.

Elimination of the duties on rice exports to Canada would be particularly beneficial to the industry. First, the elimination of duties should lower consumer prices, which in turn should stimulate demand for U.S. products. We have the capability of meeting any increase in demand resulting from such reduced prices. Second, the elimination of duties on U.S. exports should help us compete with Thailand, which steadily has been increasing exports of its lower-priced, lower-quality rice to Canada. The Thai Government has been working closely with its exporters to help them increase their rice exports to all markets. Through a number of programs that effectively subsidize exports, the Thais continue to increase their world market share, including their share of the Canadian market. Finally, a healthier trading relationship with Canada should provide benefits for the economy as a whole.

We recognize that the inclusion of some or all agricultural products will raise sensitive issues during the negotiation of the agreement. The benefits of providing duty-free treatment on rice and rice product exports are readily apparent. If agricultural commodities and products ultimately are included within the scope of the agreement, we support the inclusion of rice and hope that it receives the most favorable duty treatment afforded any other commodity or product.

THE RICE MILLERS' ASSOCIATION

MEMBERS OF
THE RICE MILLERS' ASSOCIATION

1. Affiliated Rice Milling, Inc.
Subsidiary of Rice Belt Warehouse, Inc.
Box 1446
Alvin, TX 77512-1446
(713) 331-6176

2. American Rice, Inc.
Box 2587
Houston, TX 77252
(713) 869-8241

3. Beaumont Rice Mills, Inc.
Box 3111
Beaumont, TX 77704
(409) 832-2521

4. Broussard Rice Mill, Inc.
Box Drawer 160
Mermentau, LA 70556
(318) 783-1915

5. Busch Agricultural Resources, Inc.
Jonesboro, AK 72401
Mailing address: One Busch Place, St. Louis, MO 63118
(314) 577-3347 (MO)
(501) 932-5484 (AK)

6. Comet Rice, Inc.
Box 1681
Houston, TX 77001
(713) 447-7423

7. Conrad Rice Mill, Inc.
Box 296
New Iberia, LA 70560
(318) 364-7242

8. Coors Food Products Company
Roberts Rice Mill Division
Box 337
Weiner, AK 72479
(501) 684-7321

9. Cormier Rice Milling Co., Inc.
Box 152
DeWitt, AK 72042
(501) 946-3561

10. Cotra Rice, Inc.
McGehee, AK 71654
Mailing address: Box 19567, Houston, TX 77224
(501) 222-6141 (AK)
(713) 461-6495 (TX)

11. Doget's Rice Milling Co.
795 South Major Drive
Beaumont, TX 77707
(409) 866-2297

12. Dore Rice Mill, Inc.
Box 461
Crowley, LA 70526
(318) 783-3372

13. El Campo Rice Milling Company
Box 110
El Campo, TX 77437
(409) 543-2741

14. Farmers' Rice Cooperative
Box 696
West Sacramento, CA 95691
(916) 371-3100

15. Farmers Rice Milling Co., Inc.
Box "D"
Lake Charles, LA 70601
(318) 433-5250

16. C.E. Grosjean Rice Milling Co.
1875 Marin Street
San Francisco, CA 94124
(415) 647-0268

17. Howell Enterprises, Inc.
Box 879
Forrest City, AK 72335
(501) 633-3270

18. Koda Farms, Inc.
Box 88
South Dos Palos, CA 93665
(209) 392-2191

19. Liberty Rice Mill, Inc.
Box 218
Kaplan, LA 70548
(318) 643-7175

20. P & S Rice Mills, Inc.
Box 55040
Houston, TX 77055
(713) 681-9251

21. Pacific International Rice Mills, Inc.
Box 652
Woodland, CA 95695
(916) 666-1691

22. Pioneer Foods
Division of The Pillsbury Company
Box 231
DeWitt, AK 72042
(501) 946-3546

23. Producers Rice Mill, Inc.
Box 461
Stuttgart, AK 72160
(501) 673-4444

24. Rice Growers Association of California
Box 958
Sacramento, CA 95804
(916) 371-6941

25. Riceland Foods
Box 927
Stuttgart, AK 72160
(501) 673-5500

26. Riviana Foods Inc.
Box 2636
Houston, TX 77252
(713) 529-3251

27. Supreme Rice Mill, Inc.
Box 490
Crowley, LA 70526

28. Uncle Ben's, Inc.
Box 1752
Houston, TX 77251
(713) 674-9484

ROHM AND HAAS COMPANY'S COMMENTS ON

S. 2232

- a bill to provide for the temporary suspension of the duty on mixtures of mancozeb, dinocap, stabilizer and application adjuvants.

A DESCRIPTION OF THE PRODUCT AND ITS USES

Dikar is a registered trademark of Rohm and Haas Company for a mixture of mancozeb (a coordination product of zinc ion and manganese ethylenebisdithiocarbamate), dinocap (a mixture of 2,4-dinitro-6-octyl phenyl crotonate, 2,6-dinitro-4-octyl phenyl crotonate and nitrooctyl phenols), stabilizer and application adjuvants.

Dikar is a broad spectrum fungicide-miticide used exclusively on apples to suppress mites and to control all of the major apple diseases including apple scab, powdery mildew, cedar apple rust, fly speck, sooty blotch and black, bitter and brown rot.

Dikar is imported as a finished product ready, after the addition of water, for application to crops in the field.

OTHER END USES

To our knowledge, there are no commercial end uses for Dikar other than as an agricultural fungicide-miticide for use on apples.

LOCATION OF PRODUCTION FACILITIES

The mancozeb component of Dikar is manufactured in Lauterbourg, France by a wholly owned subsidiary company, Rohm and Haas France. The dinocap component of Dikar is manufactured in Mozzanica, Italy, by another wholly owned subsidiary company, Rohm and Haas, Italia. Dikar is formulated in the Lauterbourg facility by blending mancozeb and dinocap with stabilizer and application adjuvants.

U.S MANUFACTURERS

Rohm and Haas Company was the only U.S. manufacturer of Dikar until 1985 when it ceased production here. Today (1986), there are no U.S. manufacturers of Dikar. Therefore, it is neither necessary nor desirable to continue to maintain a tariff on this product to protect the America industry.

When Rohm and Haas Company discontinued production of Dikar in the United States, all employees involved in the manufacture of this product were reassigned to other production units within the Company. Thus, no jobs were lost when production was transferred overseas.

COMPETITIVE PRODUCTS

There is no single product manufactured or sold in the U.S. that is a direct replacement for Dikar. Whereas several domestically produced materials control one or more of the pests against which Dikar is effective, no single product is as effective against such a broad spectrum of fungi and mites.

Specifically, the properties of Dikar that make it unique for pest control are as follows:

> Resistance: Most of the alternatives to Dikar are narrow spectrum fungicides with specific sites of physiological activity against the pests that they control. These specific materials used for apple scab, powdery mildew and mite control have resulted in disease or mite resistance which necessitates tank mixing of sometimes undesirable, or highly toxic pesticides. This causes the grower to resort to complex and expensive programs to compensate. Resistance to Dikar has never been documented against any disease or mite for which it is recommended: e.g., powdery mildew, apple scab, cedar apple rust, black rot, brown rot, fly spec, sooty blotch, bitterrot and mites (Schoene, European Red, two-spotted and clover).

Safety to Insect and Mite Predators: When used in a full season protective spray program, Dikar suppresses mites and prevents or delays early season infestations. This delays or prevents the need for the use of other insecticides that are toxic to mite and insect predators; making Dikar the cornerstone for integrated pest management systems. The net result is that less of the highly toxic or persistent chemicals have to be used. This makes pest control less expensive and more efficient, and greatly simplifies spray schedules. There is, therefore, less exposure of the consumer to highly toxic pesticides and reduced probability of error that may result when many pesticides are mixed in the same spray tank.

PRESENT TARIFF CLASSIFICATION AND DUTY RATE

Item 408.38, TSUS - (Subpart C, part 1, schedule 4)

"Products obtained, derived or manufactured in whole or in part from any product provided for in Subpart A or B of this part:

Pesticides:
    Other:
        Other:............................ 0.8¢ per lb. + 9.7% ad valorem"

REVENUE IMPACT OF PROPOSED SUSPENSION OF DUTY

The revenue that would be foregone as a result of the proposed suspension of the duty on Dikar is estimated to be approximately $300,000 per year for the period 1986 through 1990.

Profile for Dikar$^{(R)}$

Disease Control	The combination product, Dikar, a mixture of mancozeb and dinocap, controls a broad-spectrum of fungal diseases as well as many mites. This results in reduced usage of complex and sometimes highly toxic tank mixtures.
Toxicology	The toxicological characteristics of mancozeb and dinocap have been thoroughly studied. The use of the combination product poses virtually no risk to consumers. In addition, it poses virtually no risk to the environment since they are biodegradable and do not accumulate or carry over in the soil/water/air or food chains.
Pest Resistance	Target fungi and mites have never developed resistance to either mancozeb or dinocap, respectively, over the many years that these materials have been used.
Safety to Predators	Safety to mite and insect predators means that less total pesticide need be used. Such safety forms the basis for integrated pest management systems aimed at minimizing the use of pesticides on all crops.
Safety to Crops	When used as directed, Dikar is safe to registered crops.
Compatibility	Dikar is compatible with most of the other pesticides used for disease control in apples. Where tank mixes are necessary, it represents an efficient, cost effective basis for spray programs.
Cost/Performance	Use of a single package product with broad-based disease and mite activity results in a simplified, highly cost effective basis for pest control.

TESTIMONY OF SIECOR CORPORATION
BEFORE THE
SUBCOMMITTEE ON INTERNATIONAL TRADE
COMMITTEE ON FINANCE
April 16, 1986

This statement is submitted to the Subcommittee on International Trade, Committee on Finance by Siecor Corporation to express its views regarding the proposed initiation of bilateral negotiations between the United States and Canada on a comprehensive free trade arrangement. Siecor Corporation ("Siecor"), located in Hickory, North Carolina, is one of the largest producers of optical cable in the world. Siecor produces a full line of optical cable adaptable for use in all of the principal fiber optic markets. Siecor urges that optical fiber and optical cable used for telecommunications purposes be excluded from any negotiations for tariff concessions between the United States and Canada unless the Government of Canada makes a clear and unambiguous commitment to negotiate the elimination of all non-tariff barriers to the sale of these articles by U.S. producers in the Canadian markets.

There are two general considerations that prompt Siecor to take this position. First, the telecommunications market in Canada is only one-tenth the size of that of the United States. Thus the opportunities made available to Canadian producers by virtue of any "mutual" tariff concessions are likely to be significantly greater than the opportunities made available to U.S. producers by virtue of corresponding concessions. Second, unlike the United States telecommunications equipment market, where the recent divestiture of the Bell Operating Companies by AT&T has opened their procurement process to unrelated producers, the Canadian telecommunications equipment market is not genuinely open to non-Canadian producers Bell Canada's procurement practices closely parallel those of the Bell System prior to divestiture. This vertical integration of the largest portion of the Canadian market, coupled with the strong "Buy Canadian" preference held by Canadian telecommunications service providers, substantially limits the opportunities that would be available to U.S. producers even if major tariff concessions were made by the Government of Canada. By contrast, tariff concessions made by the United States would be immediately beneficial to Canadian producers who have free access to the United States market and who presently enjoy a substantial exchange rate advantage over their U.S. competitors.

In these comments we will first describe the importance of fiber optic technology to the telecommunications industry. We will then compare the markets for fiber optic technology in both Canada and the United States. We will demonstrate that the opportunities open to Canadian producers in the U.S. market are considerably greater than the corresponding opportunities available to U.S. producers in the Canadian market. We will then demonstrate that the structure of the Canadian telecommunications equipment market, coupled with officially approved preferences for Canadian producers, substantially limit the already small opportunities for U.S. producers in Canada. We conclude that mutual tariff concessions would substantially disadvantage U.S. producers unless the Canadian Government eliminates non-tariff barriers which currently prevent open, fair and competitive procurement by Canadian telecommunications service providers.

I. OPTICAL COMMUNICATIONS

Optical communication is presently revolutionizing the United States telecommunications industry. The installation of fiber optic communications systems is expected to continue its dramatic growth for several decades. In order to appreciate the strategic importance of the new technology and the implications of trade negotiations with Canada on America's role as the world leader in this technology, some general background on fiber optics and its use in telecommunications would be useful.

Most modern forms of communication, from the telegraph and telephone to radio and television signals, involve the movement of an electric current through a wire or electronic impulses through the air. With the invention of the laser about 1960, the possibility of communicating with a beam of light became theoretically possible. The opportunities opened by the use of light waves for communication were quickly recognized as enormous. "Communicating on a Beam of Light," Fortune (Mar. 1973) at 1.

Light waves are a part of the spectrum of electromagnetic energy which is at the heart of all electronic signal transmission phenomena, including electric current, radio waves, infrared radiation, visible light, ultraviolet radiation, X-rays, etc. The use of electromagnetic energy for communication began with the telegraph. From there, engineers began the climb up the frequency spectrum, starting with voice frequencies on telephone lines, thence to radio and television, and finally to microwaves, which carry a broad range of modern electronic communications.

The technological breakthrough by Corning Glass Works which made possible optical communications over glass fibers has been referred to by scientists as the most significant advance since the introduction of the transistor in the early 1950's. Today, one optical communications fiber only .005 inches in diameter -- about the size of a human hair -- can replace cables of copper wire several inches in diameter. In addition to the basic savings in materials that this makes possible, there are even more significant benefits resulting from the physical properties of glass and light transmission.

The transition to fiber optic transmission systems is already well under way in the interexchange portions of the network. Local exchange carriers are rapidly extending their use of these systems in subscriber feeder applications as they expand and modernize their facilities. However, widespread use of fiber in distribution plants (the crucial "last mile" of the loop between the subscriber and the central office) will be necessary before society can fully realize the potential benefits made possible by the abundance of transmission capacity being made available at higher levels of the network.

The emergence of digital switching and transmission equipment have made it possible to integrate voice, data and video signals economically over a single transmission link or "pipeline." The emergence of fiber optic cable as the premier transmission medium is creating a pipeline of enormous capacity for digital transmission of these integrated voice, data and video signals. During the next decade, the U.S. will enter an era of integrated optics whose impact on our society will be akin to that of integrated circuits. The combination of optical transmission and digital signals has positioned the telecommunications industry on the threshold of a new era. The new era will be characterized by the availability of a much wider range of high quality, reasonably priced services over the basic telecommunications network than has ever been available in its past.

The enormous transmission capacity of optical cable will allow individual subscribers to enjoy a virtually unlimited channel of communications for voice, data and video signals over a broadband, digital transmission system. The benefits that such a system will hold for both residential and business subscribers are substantial. A single fiber will accommodate simultaneous delivery of a wide array of services, including high definition television, high fidelity audio, narrow band ISDN channels for voice and data, and numerous telemetry channels for monitoring utilities, security devices, fire alarms, medical equipment, etc.

II. THE UNITED STATES MARKET FOR FIBER OPTICS

A. Size and Types of Markets

The United States market for fiber optic products is the largest in the world. It has experienced rapid growth in recent years. This growth has been led largely by the demand for optical cable in the telecommunications segment of the market. While the size of the United States market as a percent of the world market will decline over the next several years as demand for fiber optic communications in other parts of the world grows, the United States market will represent more than 50 percent of the worldwide market until 1987. The United States Department of Commerce has made the following estimate of the United States and world markets for fiber optic systems:

Table II-1
FIBER OPTICS MARKET
(Fiber, Cable and Electronics)
(Millions of Dollars)

	U.S.	World
1981	$ 190	$ 290
1982	290	450
1983	400	625
1984	560	900
1985	725	1,225
1986	880	1,600
1987	1,135	2,110
1988	1,450	2,670
1989	1,650	3,200

Source: United States Department of Commerce, International Trade Administration, A Competitive Assessment of the U.S. Fiber Optics Industry 1 (1984) (hereinafter "Competitive Assessment").

The ITA's projection of the United States and world markets is generally consistent with projections made by Kessler Marketing Intelligence ("KMI"), a well-respected consulting firm located in Newport, Rhode Island. As the following table illustrates, KMI's estimate is only slightly below that made by the ITA:

Table II-2
KMI's 1983 FORECAST FOR FIBER OPTIC MARKETS
(in $ millions)

	U.S.	World
1981	$ 90	$ 177
1982	180	327
1983	300	550
1984	400	761
1985	550	1,057
1986	750	1,429
1987	940	1,891
1988	1,200	2,432
1989	1,450	3,044

Source: Kessler Marketing Intelligence, Summary Report on Fiberoptic Markets in the U.S. 5 (1984) (hereafter "KMI").

KMI estimates that optical cable will represent approximately 71 percent of the total market in 1989.

Telecommunications represents the largest segment of the United States optical cable market. This market segment is driven by technological improvement and rapidly falling prices. The price per fiber meter of optical cable has fallen from approximately $5.00 in 1977 to below $0.50 in 1985. The price of cable will continue its downward path as volume of production increases and costs fall.

To date, the market for optical cable in telecommunications has centered on long distance lines. See "The Coming Glut in Phone Lines," Fortune (Jan. 7, 1985) at 96. The technology that will allow fiber optic cable to be run directly to subscribers is close at hand. There are no major technical hurdles left to overcome. When existing technology is reduced to cost effective practice and the demand for additional bandwidth for residential service grows, the market for optical cable for the so-called "subscriber loop" will surge dramatically. In the not too distant future the cost of using fiber optic facilities in the subscriber loop will be price competitive with todays copper based system.

In 1983, Gnostic Concepts, Inc., a San Mateo, California consulting firm, estimated that the quantities of optical fiber used in subscriber feeder loops and subscriber local loops would expand dramatically prior to 1990. As the following table illustrates, this expansion will be both on an absolute basis and as a percentage of fiber used in all telecommunications systems.

Table II-3
QUANTITIES OF FIBER IN TELECOMMUNICATIONS SYSTEMS
(In Thousands of Fiber-Kilometers)

Functional Category	1983	1987	1990
Long Haul (including undersea cable)	126	564	1,397
Interexchange and Entrance Links	71	296	562
Subscriber Feeder Loop	16	126	750
Subscriber Local Loop	4	52	1,165
Total Telecommunications System	217	1,038	3,874

Source: Gnostic Concepts, Inc., Fiber Optics Industry Service 1983 Data Base Analysis 3-9 (hereinafter "Gnostics").

Note that fiber used in the subscriber feeder loops and the subscriber local loops is projected to grow from approximately nine percent of total telephony fiber consumption in 1983 to approximately 50 percent in 1990, while the overall market expands to 18 times its original size. Combined shipments of optical cable for the subscriber feeder loop and the subscriber local loop markets have, to date, exceeded Gnostic Concept's 1983 projections. Although the growth in the total market for optical cable has been impressive to date, it is clear from the size of the anticipated future growth that fiber optics is indeed an embryonic industry with enormous potential for growth.

B. Consumers of Fiber Optic Cable

Telephony is by far the largest market for fiber optic cable. Following the divestiture of AT&T, the telephony market is now comprised of the seven regional telephone companies ("RBOCs"); independent telephone companies such as GTE, Continental, United Telecom, Centel, ALLTEL and other small independents; and other common carriers, including AT&T Communications (formerly AT&T Long Lines), MCI, Western Union, U.S. Sprint, SNET/CSX Lightnet and other long distance carriers. Most of the sales of fiber optic cable in recent years have been in the long distance trunk line market. In addition to AT&T, other providers of long distance services are turning to fiber optic systems.

The greatest opportunities for market expansion in fiber optic systems beyond the late 1980's lies in local area networks ("LANs") and subscriber loops. The major consumers of cable in this case will be the recently divested RBOCs and independent telephone companies. These companies are very cost-conscious in their purchasing decisions.

The potential for combining LANs, CATV and datacom systems in a single optical fiber system offers tremendous growth opportunities for the industry. While competition promises to be intense, no dominant supplier is readily apparent. Success in this type of market will depend largely on the abilities of suppliers to produce quality optical cable at competitive prices.

The United States market for optical fiber and cable is highly competitive. As described above, Corning Glass Works developed the breakthrough technology for making optical fibers suitable for communications applications. Corning has become one the leading producers of optical fiber in the world. In addition to Corning, the U.S. market is presently being supplied by no less than three of the largest producers of telecommunications equipment in the world. AT&T, which is estimated to be one of the largest producers of optical fiber, is an integrated producer of both optical fiber and fiber optic cable. International Telephone & Telegraph ("ITT") produces both optical fiber and cable in the United States. ITT has acquired Valtec, a firm which is estimated to have the third largest production capacity for optical fiber in the United States. Northern Telecom Ltd., a major Canadian producer of optical fiber and cable, presently markets aggressively in the United States.

Siecor is a major producer of fiber optic cable, producing cable for all five major market segments. General Cable, which has been a major manufacturer of telecommunications cable for many years, has expanded into fiber optic cable. Lightwave-Ericsson, which is a joint venture of Atlantic Richfield and L.M. Ericsson of

Sweden, also sells fiber optic cable in the U.S. market. In addition to these, there are several smaller specialized manufacturers in the United States.

C. Market Access and the Regulatory Environment

The United States market for telecommunications equipment is the largest in the world, accounting for 32 percent of worldwide telecommunications industry shipments. "Changes in the U.S. Telecommunications Industry and the Impact on U.S. Telecommunications Trade," Inv. No. 332-172, USITC Pub. No. 1542 (1984) at 18. By any standard, the United States equipment market is an open market. The divestiture of AT&T has wrought major changes in services and in procurement patterns. Prior to divestiture, a sizable portion of the United States telecommunications equipment market was captive. Following divestiture, the BOCs adopted open and competitive procurement policies. It is not certain at this point what types of long-term supplier patterns and relationships will emerge.

Between 1978 and 1984 import penetration of telecommunications equipment rose from 3.0 percent to 10.8 percent. Id. Despite the fact that United States equipment manufacturers are often in the forefront technologically, United States exports as a share of foreign consumption were less than four percent in 1983. Id. at xii. In 1985 the United States experienced a net trade deficit in telecommunications equipment as a direct result of the relative openness of our market.

Imports of fiber optic cable from Canada increased significantly between 1980 and 1985. Table II-2 illustrates tne increase in imports of optical cable from Canada.

Table II-4
CUSTOMS VALUE OF U.S. IMPORTS OF OPTICAL CABLE
(TSUSA NO. 708.2900 1980-1984; TSUSA No. 707.9010 1985)
FROM CANADA, 1980-1985
(value in $ thousands)

	1980	1981	1982	1983	1984	1985
Canada	35	30	374	5,108	14,952	22,287
Canada 1/	--	--	335	1,740	9,910	43,923

1/ Imported under tariff provision 807.00 ("assembled [in Canada] in whole or in part of fabricated components, the product of the United States . . . .").

Source: U.S. Bureau of the Census, Dep't of Commerce, Report IM-146 (Dec. 1980, 1981, 1982, 1983, 1984, 1985).

In 1985, the value of total imports of optical cables from Canada represented nearly 56 percent of the value of all United States imports of these products.

Foreign based optical fiber and cable manufacturers have announced that they will build plants in the United States to supply the United States market. Sumitomo's plant in Raleigh, North Carolina is in production. Fujikura, a Japanese fiber optic cable manufacturer, announced that it will build a plant in South Carolina as part of a joint venture with Alcoa. The Charlotte Observer (Dec. 12, 1984) at 7B. Another Japanese producer, Furakawa, is also known to be planning to build a plant in the United States in the near future. This activity illustrates the relative openness of the United States market vis-a-vis foreign markets including Canada, which are usually characterized by "buy national" policies, captive suppliers, directed procurement, or a combination of these practices, the sum of which precludes U.S. suppliers.

III. THE CANADIAN MARKET

A. The Size of the Market

Canada's population is roughly 1/10th that of the United States. The U.S. International Trade Commission estimated the apparent consumption for the total United States telecommunications equipment market in 1983 to be $18.5 billion as compared to only $1.2 billion for Canada. "Changes in the U.S. Telecommunications Industry and the Impact on U.S. Telecommunications Trade," Iv. No. 332-172, USITC Pub. No. 1542 (June 1984) at 19 (Table 4) and 38. The combined United States market in 1983 for transmission equipment, cable, wire and lightguide was estimated to be $6.9 billion, Id. at

20 (Table 5) and 23 (Table 8), as compared to a market of $424.6 million for the same articles in Canada. Id. at 39.

KMI estimates that the total Canadian market for fiber optic communications equipment in 1983 was $43 million, and that the market will grow to $95 million by 1990. KMI at 62. This contrasts with a $300 million United States market in 1983 and a projected $1.450 billion market by 1989. Id. at 9. Telecommunications applications represent approximately 97 percent of the Canadian fiber optics market.

The major Canadian telephone companies have been moving heavily toward the use of fiber optic systems since 1982. The Canadian service providers decided that, beginning in 1984, they would use fiber optic systems rather than copper wire for all trunk lines and interoffice links. KMI at 63. The companies have also begun to move toward the use of fiber optics in subscriber loops, especially for providing CATV and datacom services. Id. This movement parallels similar developments in the United States market.

One of the earliest fiber optic systems installed was the Broadband Network ("BBN"), extending 3,200 km across Saskatchewan. The system connects approximately 530,000 people in 50 cities and towns throughout the province, providing telephone, CATV and datacom service. KMI at 63-4. The provinces of Quebec and Alberta also have, or are installing, major fiber optic systems.

In addition to the data services provided on LANs, several data link systems have been installed for Hydro-Quebec, the electric power supplier to Quebec Province. KMI at 65. Several industrial applications of fiber optics, including experimental shipboard systems and a papermill in Quebec, have also been installed. The Canadian Ministry of Transportation has also installed fiber optic systems at airports. Id.

B. Consumers of Optical Cable

The Canadian telephone carrier companies are organized largely along provincial lines. The regulatory structure consists of a patchwork of national, provincial and municipal regulatory bodies as shown in Table III-1.

Table III-1
MAJOR CANADIAN TELECOMMUNICATIONS CARRIERS AND THEIR REGULATORY AGENCIES

Carrier	Regulatory Agency
Bell Canada	Canadian Radio Television and Telecommunications Commission (CRTC)
British Columbia Telephone Co.	
CNCP Telecommunications	
Telesat Canada	
NorthwesTel	
Terra Nova Telecommunications	
Alberta Government Telephones	Alberta Public Utilities Board
Saskatchewan Telecommunications	See Note 1
Manitoba Telephone System	Manitoba Public Utilities Board
New Brunswick Telephone Co., Ltd.	New Brunswick Public Utilities Board
Maritime Telegraph & Telephone Co.	Nova Scotia Public Utilities Board
Island Telephone Co., Ltd.	Prince Edward Island Public Utilities Commission
Newfoundland Telephone Co., Ltd.	Newfoundland Public Utilities Board
Edmonton Telephones	City of Edmonton
Northern Telephone	Ontario Telephone Service Commission
Quebec Telephone	Regie des services publics du Quebec
Telebec Ltee	Regie des services publics du Quebec
Teleglobe Canada	See Note 2
Thunder Bay Telephone System	City of Thunder Bay

Note 1: Saskatchewan Telecommunications is not presently regulated by an independent agency, but is owned and subject to control by the Saskatchewan government. In July 1982, the Saskatchewan government passed an act to establish a Public Utilities Review Commission. As of September 1982, the act had not come into effect.

Note 2: Teleglobe Canada is not regulated by an independent agency, but is owned and subject to control by the federal government.

Source: United States Department of Commerce "Telecommunications Policies in Seventeen Countries: Prospects for Future Competitive Access" (hereinafter "NTIA Report") at 72.

Bell Canada operates principally in Ontario and Quebec. The structure of Bell Canada closely resembles that of AT&T prior to divestiture. Bell Canada owns both a research laboratory, Bell Northern Research and an equipment manufacturer, Northern Telecom Limited (NTL). The procurement patterns of Bell Canada reflect the close relationship to its captive supplier NTL, and parallel those of the former Bell System/Western Electric relationship.

C. The Regulatory Environment and Market Access

Canada has two national telecommunications systems, the TransCanada Telephone System ("TCTS") and CNCP Telecommunications ("CNCP"). TCTS is an association of the largest telephone company in each province plus Telesat Canada. The members of TCTS are as follows:

British Columbia Telephone Co.
Alberta Government Telephones
Saskatchewan Telecommunications
Manitoba Telephone System
Bell Canada
New Brunswick Telephone Co., Ltd.
Maritime Telegraph and Telephone Co.
Island Telephone Co.
Newfoundland Telephone Co., Ltd.
Telesat Canada

NTIA Report at 73. CNCP is a partnership of the Canadian National Railways (government-owned) and the privately owned Canadian Pacific Ltd. Id. at 74. The two systems account for approximately 93 percent of the total Canadian market.

Bell Canada, which has a relationship with NTL similar to that between Western Electric and the Bell System prior to divestiture, directly controls 58 percent of all telephones in Canada. In addition, Bell Canada has significant direct and indirect equity interests in New Brunswick Telephone, Newfoundland Telephone, Island Telephone and Maritime Telegraph and Telephone Co. The second largest telephone company in Canada (11 percent of all telephones) is British Columbia Telephone Co., which is indirectly owned and controlled by GTE.

Alberta Government Telephones, Saskatchewan Telecommunications and Manitoba Telephone System are owned by their respective provincial governments. NTL has established manufacturing facilities in both Alberta and Saskatchewan, making it the "favorite son" of these government-owned operating companies.

NTL was established in 1914 as a subsidiary of Western Electric Company (44 percent) and Bell Canada. In 1956, Western Electric and Bell Canada were separated under the terms of a consent decree arising out of antitrust enforcement litigation between the United States Department of Justice and AT&T. As of January 3, 1986, Bell Canada Enterprises, Inc. held 60,647,674 shares (or 52 percent) of NTL common stock. Northern Telecom Limited, Securities and Exchange Commission, Form 10-K (1985) at 1 (hereinafter "NTL 10K"). NTL is a world leader in telecommunications and data equipment manufacturing, making a full line of telephone and data equipment. In 1985, the company had total sales of $5.8 billion (Can.). All types of wire and cable represented $360 million (Can.) up 17 percent over 1984. Id. at 14-15.

Because of Bell Canada's majority ownership of NTL, the two companies maintain a very close relationship. Bell Canada uses equipment manufactured by NTL which is based on designs developed by another subsidiary, Bell-Northern Research ("BNR"), which is jointly owned by NTL and Bell Canada. This structure parallels that of AT&T, Western Electric and Bell Laboratories prior to the recent breakup of AT&T. The links between NTL, Bell Canada and BNR are further reinforced by interlocking directorships and mobility among the companies, especially at the senior management level. NBI at 17.

Northern Telecom, Inc. ("NTI") is the wholly-owned United States subsidiary of NTL. NTI markets a much smaller product line in the United States than NTL's line in Canada. NTI focuses on items specifically targeted for the United States market. NBI at 20. NTL intends to capitalize on its strong technological position to become the leading end-to-end supplier of digital switching services in the 1980's. NBI at 6.

In the fiber optics area, NTL produces both optical fiber (under license from Corning Glass Works) and optical cable at its plant in Saskatoon, Saskatchewan. The company supplies more than 80 percent of the Canadian fiber optic market. KMI at 65.

In 1985, the United States market accounted for approximately 67 percent of NTL's total revenues, having grown from approximately 41 percent of total revenues in 1981. The substantial growth of NTL's revenue attributable to the United States market illustrates the importance of this market to the company. NTL has focused on the United States market as its largest source of potential growth in equipment sales.

NTL is an aggressive competitor with substantial designs on the United States market. The Saskatoon Star-Phoenix reports that the United States "is still the prime international market and the area where Northern Telecom feels the most significant growth can be achieved." Saskatoon Star-Phoenix (June 14, 1984) at 8.

Telephone carriers other than Bell generally split their orders for cable among suppliers which manufacture in Canada. NBI at 101. Federal and provincial government purchases of telephone equipment have not been included under the Government Procurement Code of the GATT. The Agreement on Government Procurement, Agreement Reached in the Tokyo Round of the Multilateral Trade Negotiations, Message from the President of the United States: The Texts of the Trade Agreements Negotiated in the Tokyo Round of the Multilateral Trade Negotiations . . . (June 19, 1979). In addition, the Canadian government has publicly encouraged the private sector to "Buy Canadian" in telecommunications equipment purchases.

A. The Benefits for Canada Versus the Cost for the United States

1. The Benefits Associated with a Mutual Reduction in Trade Barriers on Optical Cable Are Inherently More Favorable to Canada

As noted previously the United States market for telecommunications products generally, and optical cable specifically, is much larger than the Canadian market. Any bilateral reduction in trade barriers is thus inherently more beneficial to Canadian producers. The projected market for optical cable in the United States through 1989 is easily 10 to 15 times the size of the corresponding market in Canada. Assuming that a mutual reduction or elimination of trade barriers on optical cable achieves the intended result of opening both markets, the potential prize for Canadian producers is several orders of magnitude greater than that for their American counterparts. The relative size of the United States and Canadian telecommunications markets is so different one must question the wisdom of any bilateral discussions. It is difficult to imagine what concessions Canada could make that would sufficiently compensate for a grant of unrestricted access to the vast and expanding market for optical cable in this country.

2. Unrestricted Access to the United States Market for Canadian Producers Would Reduce the Volume of Sales for American Producers and Impair Their Cost Structure

In order to compete successfully over the long term in fiber optic communications, manufacturers must participate fully in the early development, production and installation of optical fiber systems. Those who are not able to participate in the early stages of this emerging market will not benefit from the well-known "experience curve" phenomenon. It is most unlikely that such firms will be able to compete successfully over the long term with low cost suppliers who win the race down the experience curve.

Although the domestic market for optical cable has grown significantly over the past two years, it is important to realize that as discussed supra, really dramatic growth in the fiber optic industry will likely take place several years hence. Today's market for optical cable is largely aimed at replacing or supplementing long distance lines with fiber optic systems. Future demand will, however, be based on the penetration of fiber optic cable into the lower levels of the telecommunications network.

This demand for fiber in the subscriber loop will create a market for optical cable in excess of 10 million fiber kilometers per year. Demand in the United States for fiber optic cable is expected to increase during the 1990's to an annual level in excess of 20 times that of today. It is for this future market, within the subscriber loop, that the domestic fiber optic cable manufacturers must now position themselves.

The mutual reduction of tariff barriers with Canada opens enormous opportunities for Canadian optical cable producers to participate in the large United States market and to obtain the volume needed to race their American counterparts down the experience curve. The Canadian market is, in itself, simply too small to allow NTL to develop into a world-class competitor. By contrast, even if we assume that American producers could gain access to the largely captive Canadian market, the additional incremental volume that would become available is paltry. Elimination of trade barriers with Canada at this stage of development in fiber optic telecommunications would be a strategic blunder with long-term negative consequences for American producers.

The relative benefits available from the mutual elimination of trade barriers in optical cable clearly favor Canadian producers over their American counterparts. Participation in the early stages of the rapidly expanding United States market is critical to the long-term competitive position of producers of optical fiber and cable. Volume lost to Canadian optical cable producers would weaken the competitive position of American producers not only in relation to their Canadian competitors, but in relation to all foreign producers of optical cable as well. There is no way that the Canadian government could adequately compensate the United States for facilitating the entry of Canadian producers in this market.

3. Elimination of the United States Duty Would Create a Windfall for Canadian Producers

At the present time, Canadian producers enjoy a substantial competitive advantage over their United States counterparts because of the weakness of the Canadian Dollar when compared with the United States dollar. In the event that the current rate of duty (10.0 percent) was eliminated, Canadian competitors could utilize the windfall in either of two ways:

(1) reduce prices and buy additional market share;

(2) maintain existing price levels and offset high capital and R&D costs with higher revenues or use the additional revenue to augment profits.

Siecor believes that the first option is the most likely course for Canadian producers to follow. One must believe that Canadian producers understand the experience curve phenomenon and desire to drive their own costs down by accumulating production experience through sales in the expanding United States market. If this takes place, American producers must respond by either lowering prices to defend market share or by maintaining prices (at the risk of lost sales) in order to generate the funds needed to sustain high levels of research and development and capital investment required to continue in the market.

B. Reduction or Elimination of Canadian Tariff Barriers Would Not Lead to Increased Sales by United States Producers

Tariffs represent but one relatively insignificant obstacle to U.S. firms that attempt to penetrate the Canadian telecommunications equipment market. Traditional institutional ties and relationships, as well as other non-tariff barriers, present far more subtle and ingrained barriers to U.S. producers.

Federal and provincial government purchases of telecommunications equipment are not covered by the Government Procurement Code of the General Agreement on Tariffs and Trade. This provision, which prohibits governmental entities from discriminating in favor of domestic sources of supply in procurement decisions is particularly relevant in the case of Canadian telecommunications service providers. As noted above, Canadian telephone service providers other than Bell Canada are generally owned or controlled by provincial governments. In addition, the Canadian government has publicly encouraged the private sector to "Buy Canadian" in telecommunications equipment purchases.

Market Intelligence Research Company ("MIRC") of Palo Alto, California states that "[t]rade barriers will make penetration into the Canadian marketplace for fiber optics difficult and expensive." MIRC at 118. In its assessment of NTL, Northern Business Information ("NBI") states that "[i]nstitution of competitive bidding in the Bell market will have little effect on Northern's total market share in Canada during our forecast period, if ever." NBI at 34 (emphasis added). The United States Department of Commerce notes that Northern Telecom's control of the Canadian market leaves "less than 10 percent open to others." Competitive Assessment at 31.

The fondness of the provincial governments and the Canadian telecommunications regulatory authorities for NTL is reflected in a recent proceeding before the Canadian Radio-television and Telecommunications Commission ("CRTC"). Several years ago the CRTC initiated a proceeding that would evaluate the need to protect Canadian ratepayers from the burdens of discriminatory procurement practices. In order to prevent Bell Canada from purchasing equipment from NTL at inflated prices and passing the cost on to subscribers in the form of higher rates, the CRTC proposed that the transfer price for telecommunications equipment between NTL and Bell Canada should be no higher than the price paid by any other customer (foreign or domestic) for NTL equipment. This proposal would explicitly include prices of export transactions and transfers to NTL's American subsidiary, NTI, when making comparisons with prices between NTL and Bell Canada.

The CRTC's proposal became the subject of a protracted proceeding which was finally concluded on October 5, 1984. Bell Canada - Northern Telecom Price Comparison, Telecom Division CRTC 84-23, 5 October 1984. If the CRTC's proposal had been adopted, it would have meant that NTL could not charge Bell Canada more for network equipment than it charged its U.S. customers for the same equipment. The CRTC ruled, however, that NTL need only offer Bell Canada the lowest prices available to its customers in Canada and that it would not be forced to offer Bell Canada the lower prices that it charges in export markets. Id. at 11-12.

The very existence of the CRTC proceeding illustrates the fact that telecommunications trade between the United States and Canada is essentially a one way street moving south. If the U.S. producers were allowed to compete in Canada on an equal basis, NTL would be forced to offer Bell Canada competitive prices. Bell Canada would have had no occasion to seek regulatory approval of higher home market prices. In addition, the fact that the CRTC eventually ruled that NTL need not extend competitive world market prices to Bell Canada represents nothing less than an official governmental sanction for a dual pricing system -- high prices in the protected home market and lower prices in the competitive U.S. market.

During the CRTC's proceeding, NTL itself admitted that the existing procurement practices protect integrated suppliers. In its submission to the CRTC, NTL stated: "[t]he United States and Canadian arrangements [prior to divestiture in the U.S.] result in the protection of the vertically integrated markets (described in §3.2) for the benefit of the equity related suppliers. . . ." Submission of Northern Telecom Canada, Limited to the Canadian Radio-television and Telecommunications Commission, filed September 1, 1981 at 29. NTL elaborated further on the relationship between itself and Bell Canada in a later portion of its submission:

> Northern can justify funding the development of the broad line of telecom products needed for Bell's network because it knows that Bell will buy those products, subject to the operations of the Supply Contract, on an on-going basis, whatever their life cycle stage, as long as they continue to represent good value to Bell. Without that relatively stable base market */, Northern could not continue to develop the range of products tailored to Bell's needs that Bell must have if it is to remain the leading Telco.
>
> */
>
> In working with Bell to develop the network enhancing products needed for Bell's network, Northern invests its money on an on-going basis in what are high risk undertakings. It could not responsibly do that if it did not, among other things, have a reasonable expectation

> that a sufficient volume of sales of all its products will be achieved to support that investment and produce a reasonable profit. *The relatively stable Bell market is essential to that expectation.*"

Id. at 97. (Emphasis added).

The CRTC's 1984 opinion is an extraordinary document that provides an interesting insight into the Canadian telecommunications equipment market. The CRTC's opinion makes it quite clear that Bell Canada is a captive customer, and that it procures equipment from other suppliers only when such equipment is unavailable from NTL.

> In its submission, Bell stated that it procures telecommunication products and resources from NTL under the terms of a contract (the Bell/NTL Supply Contract), which obliges NTL to supply Bell with materials it reasonably requires for its business at prices as low as those charged to NTL's most favoured customer for like products and services under comparable conditions. As NTL is Bell's preferred supplier, the Company seeks to purchase from other suppliers only when NTL is unable to supply particular types of equipment and services . . . . The Company further indicated that it determines the requirement for a product and negotiates its development and production with NTL through a multi-stage process which ultimately results in a firm price for the product.

Id. at 5. Ironically, Bell Canada argued strenuously that it should not be given the opportunity to pay lower prices to NTL because this would "cause unnecessary modifications to NTL's marketing strategy." *Id.* at 6. Such modifications would undoubtedly prevent NTL from fueling low priced exports through high prices in its protected home market.

The CRTC's opinion goes on to demonstrate how vigorously Bell Canada resisted the concept of competitive bidding.

> It was Bell's position that implementation of competitive bidding would eliminate the benefits of vertical integration. The extensive flow of proprietary information among Bell, NTL and Bell-Northern Research Limited (BNR) would have to be stopped in order to ensure that all bidders were treated equally. Bell further stated that the termination of this flow of proprietary information would prevent integrated planning as currently practiced among the three companies.

> Integrated planning and purchasing were said to be vital to the development of the Bell network and to Bell's and NTL's ability to develop products and services at "the leading edge of telecommunications" despite the relatively small size of the Canadian market. Other benefits cited included minimized investment risks, production economies and the ability to spread development costs over a longer time period.

Id. at 7-8.

NTL's submission to the CRTC reflected great apprehensions that the introduction of competitive bidding would only benefit foreign suppliers:

> NTL's submission indicated that its main competitors are foreign-owned, with the exception of producers of wire and cable and PABX equipment. In view of this, it was Bell's argument that these foreign-owned competitors would be the major beneficiaries in the opening of the Bell market to competitive bidding. Bell contended that, to these foreign-owned competitors, the Bell market would be conveniently incremental to the much larger U.S. market, due to its proximity, and the increased inflow of foreign equipment could have the effect of reducing employment in NTL's operations.

Id. at 8.

In reaching its decision, the CRTC showed no inclination to do anything that would benefit NTL's competitors in the United States. On the contrary, the CRTC explicitly stated that its decision was designed so as not to impede NTL's participation in the United States market:

> The Commission has also considered Bell's submission with respect to differing market conditions, in particular as between the U.S. and Canadian markets. The Commission agrees with both Ontario and Bell that NTL should not be unduly constrained by domestic regulation in its participation in foreign markets. The Commission subscribes to the view that the successful participation in such markets by NTL contributes to its ability to provide advanced and diverse products to Bell at reasonable price levels, which is ultimately in the interest of Bell subscribers.

Id. at 11. Thus, while the CRTC showed great concern over protecting NTL's ability to provide "advanced and diverse products" to Bell Canada at "reasonable price levels," it showed absolutely no inclination to have such products provided by other suppliers at competitive prices.

Some of the comments filed by parties to this Canadian proceeding were also very revealing. In commenting on the CRTC proposal, the Ministry of Transport and Communications of Ontario stated: "Ontario's primary concern is that the principles established by the CRTC to govern the sale price of Northern Telecom equipment to Bell Canada may have a negative effect on Northern's ability to compete effectively in foreign markets." The Ministry further noted: "The vertical relationship between Bell Canada and Northern Telecom Limited has been a matter of intense debate during many of the Bell Rate Hearings before the CRTC and its predecessors since 1921." Despite this historic concern, the Ministry concluded: "While this [the CRTC proposal] would undoubtedly ensure that Bell Canada would pay the lowest price paid to any of Northern Telecom's customers, it is Ontario's contention that the inclusion of export and intercompany transfer prices in the comparison is unnecessary and potentially harmful to Northern's competitive position in foreign markets." Letter to Mr. J.G. Patenaude, Secretary General, CRTC, from James Snow, Minister of Transport and Communications, Province of Ontario (August 31, 1981). The obvious implication of this comment is that NTL would not be able to compete effectively in foreign markets either because it would be forced to lower the Canadian price and undercut the home market profits that fuel low priced export sales, or because it would have to raise export prices to levels charged in the protected Canadian market.

In taking this position, the Ministry of Transport and Communications of Ontario defended the right of NTL to charge Bell Canada higher prices for NTL equipment than prices charged in export markets. NTL could not, of course, charge Bell Canada higher prices than it charges its U.S. customers were it not for the fact that it enjoys the position of a favored supplier and has no need to fear free competition in Canada from foreign companies.

Bell Canada's willingness to pay NTL supracompetitive prices for equipment is easily explained. Since Bell Canada is a regulated monopoly, it can bury the burdens of its discriminatory procurement practices in its rate base and pass these additional costs on to its customers in the form of higher telephone bills. From the point of view of international trade, the higher rates paid by Canadian telephone subscribers are subsidizing NTL's competitive activities in the United States market.

NTL obviously enjoys a favored position in the Canadian equipment markets. The Canadian regulatory authorities have, moreover, shown a great tolerance for NTL's need for supracompetitive prices in the Canadian market in order to permit it to compete more effectively in export markets including the United States. Under these circumstances, any mutual reduction in tariff barriers would enlarge the opportunities for Canadian producers to sell in the U.S. market without appreciably improving the competitive opportunities of U.S. producers in Canada.

IV. CONCLUSION

The relative size of the Canadian and U.S. markets creates a situation where the benefits of any free trade arrangement would be inherently more favorable to Canadian producers. Moreover, bilateral reduction of tariff barriers would do little to enhance market access for U.S. producers, because the Canadian market is dominated by a vertically integrated supplier who benefits from a long-standing, ingrained bias favoring Canadian producers.

The present structure of the Canadian telecommunications industry -- which closely resembles the pre-divestiture Bell System in this country -- coupled with the strong "Buy Canadian" bias that prevails north of the border, provides only limited export opportunities for United States equipment suppliers. Indeed, the Canadian Radio-television and Telecommunications Commission has officially sanctioned a dual pricing scheme that permits NTL to charge Bell Canada high supracompetitive prices for equipment in the protected Canadian market while it charges lower competitive prices in the United States market. Since Bell Canada passes NTL's higher prices back to its customers in the form of higher rates, Canadian telephone subscribers are, in effect, providing NTL with a subsidy to assist it in exporting to the United States.

Under these circumstances, a mutual reduction in tariff barriers between the United States and Canada would, without more, constitute a strategic blunder on the part of the U.S. government. The United States has taken giant steps in recent years to open our own telecommunications equipment market to competition. The U.S. should expect no less from the Government of Canada if it approaches the negotiating table for a comprehensive free trade arrangement. The rules of competition in Canada are quite different from the rules that now prevail in this country. The United States would be quite foolish to negotiate an unrestricted free trade arrangement with Canada unless the rules which restrict competition within Canada are changed. Siecor respectfully submits that telecommunications equipment be excluded from any bilateral trade negotiations with Canada unless such negotiations include removal of all of Canada's non-tariff barriers to trade on such products.

Siecor appreciates this opportunity to submit its views.

STATEMENT OF

VERNON T. JONES, PRESIDENT
THE WILLIAMS COMPANIES

Natural Gas Sales should be Included in the Proposed Initiation of Bilateral Negotiations Between the United States and Canada on a Comprehensive Free Trade Arrangement

I.

This statement is submitted by Vernon T. Jones, President, The Williams Companies, One Williams Center, Post Office Box 2400, Tulsa, Oklahoma 74102, (918) 588-3304.

Mr. Jones' statement is presented on behalf of The Williams Companies (TWC) and its subsidiaries. The subsidiaries with direct interests in the subject matter of the proposed U.S.-Canada free trade negotiations are Northwest Energy Company, of which Mr. Jones is President and Chief Executive Officer, Northwest Pipeline Company, and Northwest Alaskan Pipeline Company.

This statement is also presented on behalf of Kern River Gas Transmission Company (Kern River) which is a joint venture interstate natural gas pipeline project sponsored by Kern River Corporation, a wholly-owned subsidiary of Tenneco, Inc., and Williams Western Pipeline Company, a wholly-owned subsidiary of The Williams Companies.

II.
SUMMARY

On March 18, 1985, the Quebec Summit initiated a joint U.S.-Canada effort to establish a climate of greater predictability and confidence in which citizens of both countries could plan, invest, grow and compete. In pursuit of this goal, President Reagan and Prime Minister Mulroney directed that action be taken, inter alia on

> "strengthening our market approach to Canada-United States energy trade by reducing restrictions, particularly those on petroleum imports and exports, and by maintaining and extending open access to each other's energy markets, including oil, natural gas, electricity and coal."

A. The United States imports up to 1 Tcf of natural gas annually from Canada. This trade has been important and beneficial to both countries. As domestic United States deliverability surpluses diminish, Canadian natural gas will become of increasing long-term importance to the United States.

B. The history of Canadian natural gas exports demonstrates that supply disruptions and price distortions occur when either government imposes post-hoc regulations on contracts negotiated between buyer and seller.

C. The administrations of President Reagan and Prime Minister Mulroney have promulgated policies and regulatory initiatives which have created an environment in which U.S. buyers and Canadian sellers may negotiate with freedom to arrive at market-sensitive contract terms. This environment had not existed since the early 1970s. The trade agreement should preserve it.

D. The Committee should urge the United States representatives in the bilateral free trade negotiations to include within the trade agreement assurances by both governments that natural gas purchase contracts may be freely negotiated between Canadian sellers and United States buyers, and that, once submitted to and approved by regulatory authorities of both governments, the contracts be allowed thereafter to operate free from governmental interdiction of their terms.

E. The United States representatives should urge further that a mechanism be provided in any implementing legislation on the Agreement whereby regulatory bodies may regularly consult and communicate on issues of mutual interest. This mechanism does not now exist except for specialized instances.

F. With the foregoing two items added to the agenda for the U.S.-Canada Free Trade Negotiations, we urge that the Senate Finance Committee not disapprove of such negotiations as contemplated by Section 102 of the Trade Act of 1974, as amended by Section 401 of the Trade and Tariff Act of 1984.

III.

MR. JONES' STATEMENT

We appreciate the opportunity afforded us by the Committee to present our views on a subject which could be included productively in the Canadian free trade agreement.

We commend President Reagan and Prime Minister Mulroney on their initiative in commencing the process toward a meaningful agreement between Canada and the United States securing bilateral free trade opportunities for businessmen on both sides of the border.

I recognize that the focus of much of the work done to prepare for the negotiations has been on the trade in merchandise and manufactured products. A large portion of the commerce between the U.S. and Canada involves such items. I would like to call to the Committee's attention, however, and to the attention of the U.S. negotiators, the very significant purchases of Canadian natural gas by U.S. pipelines and end users. I shall use the opportunity so graciously afforded me by the Committee to speak to that subject and to set out why I believe the free trade talks should encompass natural gas.

A. Extent of the Gas Trade.

Other witnesses have pointed out that the United States and Canada are the world's largest trading partners, exchanging $120 billion of commerce annually. Natural gas sales from Canada to the U.S. currently make up roughly $4 billion of Canada's $67 billion annual total sales. The two countries have engaged in this mutually beneficial natural gas trade for over twenty years. During this time, Canadian gas exports have expanded to meet the U.S. demand as it has grown, and an efficient and economic pipeline system is in place for deliveries. It is reasonable to expect an increase in sales from U.S. sellers northward to Canada in the future. As a gas trade with Mexico matures, a North American gas market will develop.

In 1960, Canada's exports to the United States reached 160 Bcf/year. By 1970, total exports were 780 Bcf/year, and exceeded 1 Tcf/year by 1972, a level sustained for most of the next ten years. There was a decline in 1980, 1981, and 1982 to about 800 Bcf/year. This was a period when U.S. market demands receded, and Canadian gas lost market share more than U.S. production, because the governmentally mandated border price was too high. In 1985, Canadian volumes recovered to 911.3 Bcf as prices became more competitive and less regulated.

During the seventies, Canada supplied, year by year, approximately 5% of the total United States natural gas requirements. During this same period, many U.S. gas companies were forced by supply shortages to curtail deliveries to firm customers. Thus, Canada has been a consistent source of natural gas for the United States. While Canada has been fulfilling the U.S. need for large volumes of natural gas, the U.S. in return has provided Canada substantial export revenues with its gas markets. Both countries have benefitted and can continue to benefit from this relationship.

B. The Williams Companies Interest in Canadian Natural Gas Imports

As manager of a U.S. corporation with its welfare significantly tied to the energy trade between the U.S. and Canada, I am enthusiastic at the prospects of a bilateral free trade agreement between the two countries. I shall outline my company's involvement in Canadian natural gas imports.

Northwest Pipeline Company is the only pipeline serving the Pacific Northwest. It was designed and constructed to use a combination of Canadian and domestic gas for its base load supply. During the past decade, Northwest Pipeline has purchased almost 2 Tcf - nearly $6 billion - of Canadian gas from its Canadian supplier, Westcoast Transmission Company, making it the major purchaser of natural gas produced in British Columbia.

Northwest Pipeline is also a major transporter of Canadian gas consumed in the Southern California market. Using facilities constructed in 1980-81, Northwest Pipeline transports up to 240 MMcf per day of gas for Pacific Interstate Transmission Company, which purchases the gas from another TWC subsidiary, Northwest Alaskan Pipeline Company. This gas, which is produced in Alberta, is transported through the Canadian portion of the Western Leg Prebuild facilities to Kingsgate, and then transported by three pipelines - including Northwest Pipeline Company - to the California border. Since these volumes began flowing in October 1981, Northwest Pipeline has transported nearly 250 Bcf of Canadian gas, amounting to nearly $950 million of revenue for Canada. The National Energy Board has authorized the export of this gas through 1996.

Northwest Alaskan is also a major importer of Canadian gas flowing through the Northern Border Pipeline (of which TWC is an owner) to markets in the Midwest and Southeast U.S. This Canadian gas is produced in Alberta and purchased from Pan Alberta, Ltd. by Northwest Alaskan. The gas is transported to Northern Border by two Canadian pipeline companies, NOVA and Foothills, to Monchy, Saskatchewan. Northwest Alaskan resells this gas for system supply to Northern Natural Gas Company, United Gas Pipe Line Company, and Panhandle Eastern Pipe Line Company, which are the shippers over Northern Border Pipeline. Since August 1982, when deliveries of Canadian gas through Northern Border first commenced, Northwest Alaskan's total purchases of Canadian gas for its Northern Border customers has amounted to nearly 400 Bcf, or about $1.6 billion of natural gas trade. Further, Northwest Alaskan is authorized to import up to 300 Bcf annually under its Northern Border authorization through October 31, 2002 - about twice the annual average actually moved to date. The NEB's export authorization to Pan Alberta extends through October 31, 1996.

In total, The Williams Companies subsidiaries purchased in 1985 324 Bcf of Canadian gas, accounting for roughly one-third of the total 905 Bcf of Canadian natural gas exported to the U.S.

For 1986, the combined purchases of Canadian gas by Northwest Pipeline and Northwest Alaskan Pipeline will amount to almost 300 Bcf, worth about $850 million.

While these current operations are substantial, our interest extends much further into several major projects in support of expanded U.S.-Canadian trade. One of these is the proposed Kern River Gas Transmission Company. Kern River is a joint venture by Williams and Tenneco, Inc. to build an 800-mile pipeline from an interconnection with Northwest Pipeline's facilities in Wyoming to Bakersfield, California. The pipeline will transport natural gas for use by Enhanced Oil Recovery (EOR) producers for steam injection into the heavy oil fields located in the Kern County area. The EOR natural gas market is expected to increase to well over 1 Bcf per day in the early 1990s. It is expected that Canada will provide one-half of the initial requirements (350 MMcf/d) as well as one-half of the ultimate natural gas requirement (500 MMcf/d) of the EOR producers. The project, with an estimated cost of approximately $800 million (1985 dollars), would provide Canada with an excellent opportunity to sell gas on a firm basis to a stable market over a 15-year period, thus providing a substantial cash flow to its producing provinces and increasing utilization of Canadian natural gas transportation facilities. Kern River will be a transporter rather than purchaser of Canadian gas, although Williams and Tenneco intend to serve an aggregater function, when necessary, in bundling packages of gas supplies for resale to EOR producers, who require contract security for their Canadian purchases.

C. The Experience with Regulation

Until the mid-1970's, the border price of Canadian gas was arrived at through direct buyer-seller negotiations. The cost of transporting gas through Canada to the border was established on a cost-of-service basis. Negotiations focused on the purchased gas component of the uniform border price with the object of reaching a total price responsive to the particular market in which the gas was to be sold.

In the early 1970s, the Canadian National Energy Board (NEB), the Canadian counterpart to what is now the U.S. Federal Energy Regulatory Commission (FERC), began to take a more active role in establishing the border price by announcing a policy of requiring exported gas to be priced in relation to the price of alternative fuels in the U.S. In 1973, the NEB took internal steps to encourage Canadian exporters to increase their prices. During the period from late 1974 through July 1981, the NEB, through recommendations to the Governor-in-Council, effectively set natural gas export prices. Since August 1981, however, export prices have been set by the Minister of Energy, Mines and Resources, of which the NEB is a part.

In 1975, the era of direct buyer-seller negotiations essentially ended when the NEB directed an increase in the average border price from Canadian $1.00 to $1.60 per MMBtu. Negotiated contracts not accommodating these increases were effectively overridden. Industry skepticism about contract integrity in the shifting face of government regulation can be traced to this period. In 1976, the NEB proposed further substantial increases in export prices, with different proposed border prices for each region of the U.S. The single highest border price was proposed with respect to exported volumes to be sold in the U.S. West Coast. In response to strong opposition, the U.S. Government proposed the concept of a uniform border price that lowered the cost of imported gas to California but raised the price of such gas in the Midwest and the East Coast. The Northwest Pipeline and the Congressional delegations representing Northwest Pipeline's customers objected vehemently to the uniform border price concept. Nevertheless, the concept of a uniform border price was adopted by the Canadian Government in June 1976, and has tormented the relationship until recently.

In April 1977, the NEB changed its export pricing policy by establishing the border price of Canadian exports on the basis of its "substitution value," or the cost to Canada of displacing imported crude oil in Eastern Canada with Canadian gas. This policy apparently was adopted to avoid any criticism that U.S. gas consumers were being subsidized under the old policy at the expense of Canadian gas consumers in Eastern Canada. Its effect, as was the effect of each price policy change on the part of Canada, was to increase prices. In response to the rapid increase in the price of imported oil in the late 1970's, the NEB raised the border price from $1.93 (U.S.) to $3.45 (U.S.) per MMBtu, in November 1979.

It should be noted that while unilateral Canadian decisions on import prices (with the effective cancellation of price terms in underlying contracts) were being made, the U.S. regulatory policies in effect until 1978 virtually invited that response. It was during that period that rigid wellhead prices for natural gas were promulgated by the Federal Power Commission. It is now accepted that these prices were substantially below the level the market was prepared to pay for natural gas, a situation that was not alleviated until Congress passed the Natural Gas Policy Act in 1978.

Underpriced U.S. gas supplies created a "cushion" that enabled Canadian gas prices to rise to levels a free market would not have tolerated. This over-regulation in one country spawned over-regulation in the other.

In response to the NEB's announcement in January 1980 of another increase of the border price from $3.45 to $4.47 per MMBtu, the U.S. called for government-to-government consultations. Consultations were held in February 1980. As a result, letters between Canadian Energy Minister LaLonde and U.S. Secretary of Energy Duncan were exchanged on March 25 and March 26, 1980. This exchange of letters, often referred to as the "Duncan-LaLonde Agreement," established the border price of Canadian gas on the basis of the average cost of a "basket" of a variety of crude oil imported into Eastern Canada, with certain transportation adjustments. Under this formula, the uniform border price was raised on April 1, 1981, from $4.47 per MMBtu to $4.94 per MMBtu.

With the deepening recession in 1982, and the simultaneous increase in the price of domestic natural gas generally and the increased surplus of natural gas supply, Canadian imports became uncompetitive in most U.S. markets. However, existing contractual arrangements, nonetheless forced U.S. importers to continue taking Canadian gas. In response to these problems, U.S. Government officials called for government-to-government consultations in a forum known as the U.S.-Canadian Energy Consultative Mechanism (ECM). Two ECM meetings were held on this issue, one in February 1983, and the other in September 1983.

Partly in response to these meetings, and in an effort to increase Canadian gas exports, which had fallen to 43 percent of authorized volumes, or 713 Bcf, the Canadian Government in 1983 took three distinct actions to lower the price of Canadian gas. First, in April 1983, Energy Minister Jean Chretien announced a reduction in the uniform border price from $4.94 to $4.40 per MMBtu. In July 1983, the Energy Minister implemented the Volume Related Incentive Pricing (VRIP) program, under which gas purchased above certain base volumes is discounted to $3.40 MMBTu. Finally, on November 1, 1983, the Energy Minister amended the VRIP program to provide U.S. importers greater flexibility in purchasing discounted gas.

D. Current Regulatory Environment

At no time since the flowering of natural gas regulation in the U.S. and Canada has there been a regulatory and market climate on both sides of the border that permits the current degree of contract flexibility. Until recently, the pervasive regulation of Canadian gas exports into the U.S. on both sides of the border prohibited a great deal of the flexibility and latitude that exists in the negotiation of contracts for the sale of unregulated commodities. As related above, during the ten-year period from 1974 through November 1, 1984, the NEB established both the price and the total volumes of Canadian natural gas exported to the U.S. On the U.S. side of the border, the price and other significant terms of natural gas import arrangements were again reviewed, initially by the Federal Power Commission, and more recently by the Economic Regulation Administration (ERA) and the FERC pursuant to the Department of Energy Organization Act and the Natural Gas Act (NGA).

In 1984, however, both the U.S. and Canadian governments significantly altered the existing regulatory framework by allowing the parties to a contract greater latitude in the negotiation of the price and other terms of a gas export contract. On February 17, 1984, the U.S. Department of Energy issued its "Policy Guidelines and Delegation Orders on the Regulation of Imported Natural Gas" ("Revised DOE Import Policy"). Under the new policy, the U.S. Government essentially replaced the more traditional regulatory review of import arrangements by placing greater emphasis on direct buyer-seller negotiations to arrive at competitively priced import arrangements responsive to changes in the markets served. The Revised DOE Import policy directed the ERA, in determining whether these goals were met, to examine three factors: (1) competitiveness; (2) need for the natural gas; and (3) security of supply. It is readily apparent from the Import Policy itself and from subsequent public statements by DOE officials that the "competitiveness" factor forms the cornerstone of DOE's new guidelines. The existing DOE policy guidelines explicitly require that "the terms and conditions of a gas purchase contract, taken together, must provide a supply of gas that the importers can market competitively over the term of the contract."

On the Canadian side of the border, the Canadian Government, on July 23, 1984, moved significantly in the same direction under its new natural gas export policy. Under the new export policy, which became effective November 1, 1984, exporters and importers were allowed, subject to certain limitations, to negotiate the price and other terms of an import contract. The limitations, or guidelines if you will, for the negotiating parties were, until recently:

1. The price of the exported natural gas must recover its appropriate share of the costs incurred.
2. The price of the exported gas must not be less than the wholesale price of natural gas at the Toronto city-gate and sold under similar terms and conditions, which is approximately U.S. $3.14 per million Btu (MMBtu).
3. The price of the exported gas must result in prices in the U.S. market area that are at least equal to the price of major competing energy sources, which presumably include domestic natural gas.

4. Export contracts must contain provisions that permit adjustments to reflect changing market conditions over the life of the contract.

5. Exporters must demonstrate that export arrangements provide reasonable assurance that volumes contracted for will be taken.

6. Exporters must demonstrate that producers supplying gas for an export project endorse the terms of the export arrangements and any subsequent revisions thereof.

7. Exporters must demonstrate that, where existing contracts are renegotiated, the economic return to Canada will be enhanced.

The Government of Canada, effective November 1, 1985, replaced the Toronto city-gate price floor with the requirement that net export prices be not less than the regional price to Canadians in the vicinity of the export for the same type of service. This new standard resulted in substantial reductions to the border price, particularly for exports to the West Coast. Other previously existing restrictions and limitations were also removed, thus minimizing the regulatory burdens previously borne by Canadian exporters. Spot sales by U.S. sellers to eastern Canadian markets have been initiated recently and show the promise of a future two-way trade in natural gas that will use economically the superb transmission capacity inherent in the North American pipeline systems.

The regulatory framework that now exists relies heavily upon the parties to the contract to determine price, volumes, and other terms of the import arrangement. Thus, whereas the contracting parties in the past were required to reflect regulatory policies in the terms and conditions of an import contract, it can be said today that the regulatory schemes in both countries look to the contracts to provide the regulatory details. The degree of contract flexibility that this allows likely should translate into larger volumes of Canadian gas being exported into the U.S. at competitive prices. The benefits of the new regulatory climate therefore should be felt on both sides of the border. We urge that our negotiators secure continuation of this climate through the trade agreement.

E. Contract Integrity

Pricing is the primary barrier to increasing (and/or continuing) Canadian imports. However, legal insecurity undermines the confidence of both buyers and sellers that contracts will be permitted to survive changes in market conditions. Once finalized, these contracts are subject to scrutiny and approval by the appropriate agencies in each country. While such contracts contain lengthy terms, history shows that they have not been free from subsequent governmental interference. Pricing provisions, payment mechanisms, and terms providing for priority of delivery during curtailments have been subjected to governmental intervention without notice. Such interference by either government undermines the ability of private parties to negotiate and rely on long term contracts. Accordingly, we believe that the bilateral trade agreement can and should include undertakings by the U.S. and Canada that once such contracts have received initial approval from both governments, they will not be interfered with during at least their primary term. Sound business decisions simply cannot occur in an environment where prudently entered into contractual commitments can be substantially modified or nullified by regulatory action. We believe a bilateral commitment to respect the sanctity of contracts will improve the mutually advantageous energy trade between the two countries.

The need for regulatory certainty is further underscored by financing requirements. The capital intensive nature of most new natural gas projects usually requires that a substantial portion of the project be financed through debt. Financial institutions not only look to the credit worthiness of the project sponsors, but rely heavily on binding contractual commitments to use the pipeline. Any perception that a contract might be voided, either directly or indirectly, by regulatory whim, increases the cost of financing to the sponsors and ultimately to natural gas consumers. Worse, it can result in the failure of a project altogether.

F. The Need for Mechanisms for Regulatory Consultations

While we believe that contract integrity assurances should be a fundamental part of a free trade agreement, we are not so naive as to believe that the complex regulatory apparatus on both sides of the border would be dismantled. Natural gas transactions and natural gas utilities will continue to be regulated. Our foregoing suggestion is not that regulation be abolished, but that after regulators have initially approved natural gas sales contracts, initial approval not be withdrawn.

The marketplace functions best in the absence of regulation. However, it can function efficiently under consistent and predictable regulation. We believe, therefore, that an effort should be made by negotiators to improve that consistency by providing a mechanism by which Canadian and U.S. regulators may communicate and exchange views.

Because of the direct impact of the two countries' export and import policies on trade relationships, representatives of U.S. and Canada executive departments have long recognized the need for and importance of maintaining open lines of communication and, whenever possible and appropriate, coordinating the development of their respective policies. As discussed earlier, informal and formal executive level discussions have been held under the auspices of the Energy Consultative Mechanism.

The need for a mechanism to encourage an on-going dialogue at the regulatory levels is equally important. The ratemaking and transportation policies of the NEB and the FERC have, and will continue to have, a critical role in the energy trade between the U.S. and Canada. The manner and the terms and conditions under which imported gas is ultimately flowed through to gas consumers in both countries can have as much, if not more of, an impact on energy trade and international relations as export and import policies. As energy trade between these two countries grows - and every indication is that it will - it is likely that the incidental upstream, or downstream, or "ripple", effect of the regulatory ratemaking policies of the NEB and the FERC will gain increasing significance across the border.

The effects of the regulatory policies of the FERC and NEB on energy trade, and the need to provide a consultative mechanism for these sister agencies was recognized and, indeed, implemented in the Agreement between the United States of America and Canada on Principles Applicable to a Northern Natural Gas Pipeline (Agreement on Principles). The Agreement on Principles, which was enacted into law as part of the President's Decision and Report to Congress on the ANGTS, established a general framework of cooperation between the U.S. and Canada for the construction and operation of the ANGTS. A copy of the Agreement on Principles is attached to these comments.

Paragraph 9 of the Agreement specifically provides, in addition to executive level consultations, that "the respective regulatory authorities of the two Governments will consult from time to time on relevant matters arising under this Agreement ... relating to tariffs for the transportation of gas through the Pipeline." By imposing a mandatory requirement for such periodic regulatory consultations, the President, the Congress, and the Government of Canada correctly perceived the importance of the regulatory process on international energy trade matters. With respect to issues created by the Alaskan pipeline system, the consultative process has worked on several occasions.

We believe that the inclusion of a similar regulatory consultative mechanism in any bilateral U.S.-Canada trade agreement is equally appropriate and necessary if the agreement is to be implemented fully and successfully. The consultative mechanism should provide that the "appropriate regulatory authorities of the U.S. and Canadian Governments shall consult from time to time on energy related matters subject to their jurisdiction which may affect energy trade between the U.S. and Canada." Such a provision would be in the best interests of both countries by promoting the free flow of information, and by providing a forum for the full and frank discussion of areas of mutual concern and interest.

In an era of expanding U.S.-Canadian energy trade, we believe that periodic consultations between the U.S. and Canadian energy regulators is a prerequisite to a fully informed decision-making process. Maintaining open lines of communication would, we believe, minimize, and hopefully avoid altogether, unnecessary regulatory burdens and uncertainty which could hamper the further development of export and import energy trade.

In summary, The Williams Companies strongly support and urge that the negotiators of the trade agreement consider the inclusion of a regulatory consultative mechanism. Such a mechanism is, we believe, essential to the full achievement of the purposes and goals of the proposed bilateral trade agreement.

April 16, 1986

BEFORE THE
SENATE FINANCE COMMITTEE
UNITED STATES SENATE

STATEMENT OF
JERRY K. PEARLMAN
CHAIRMAN AND PRESIDENT
CHIEF EXECUTIVE OFFICER
ZENITH ELECTRONICS CORPORATION
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(312) 391-8181

COMMENTS ON PROPOSED U.S.-CANADA FREE TRADE NEGOTIATIONS

MEMBERS OF THE SUBCOMMITTEE:

Gentlemen, I am Jerry K. Pearlman, Chairman and President of Zenith Electronics Corporation. Zenith was a founding member of the U.S. consumer electronics industry. We began in 1923 when radio was in its infancy. We have survived in recent decades despite the dumping of consumer electronics from the Far East, and remain a manufacturer of consumer electronics. Zenith has been known for years as a leading producer of color television receivers and picture tubes, and more recently as a manufacturer of computer systems and components and of microcomputers which we supply to the Internal Revenue Service, the U.S. Armed Forces, education and business markets.

Your Committee has invited comment on the potential effect a bilateral free trade arrangement between the United States and Canada may have on our industry. Zenith would welcome free trade with Canada, provided that the trade can be conducted on a fair basis between countries.

Zenith began pursuing Canadian and other foreign markets from the time the company was founded. We had sales representatives across the world in the 1930's and again in the 1950's after World War II.

In 1971, after long hard fought antitrust litigation, we overcame private restraints that permitted us and all other U.S. consumer electronics manufacturers to sell in the Canadian market. Zenith Radio Corp. v. Hazeltine Research, Inc., 401 U.S. 321 (1971). Since then we have sold millions of dollars worth of television receivers to our Canadian customers despite the fact that Canadian duty has generally been substantially higher than the U.S. duty rate on television receiver imports into the United States.

We have long believed that free trade between Canada and the U.S. would improve business for our industry in both countries, and probably would not injure the Canadian consumer electronics industry. We continue to believe that this is true but with reservations because of a radical change in both our national markets.

Over the last twenty years Japanese manufacturers, and more recently the Koreans, with their constant dumping of television receivers and picture tubes, have so seriously impaired the North American consumer electronics industry that few original members survive in the United States and even fewer in Canada.

Given an industry now nearly controlled by the Japanese and Koreans, we are concerned that unless carefully drafted a bilateral, free trade arrangement between the United States and Canada could result in a new dumping opportunity for Japan and Korea without commensurate trade concessions from these countries.

A substantial tariff differential exists between the United States and Canada which the Japanese and Koreans could exploit without adequate safeguards in the proposed United States/Canadian arrangement. When the Tokyo round concessions are fully phased in, the Canadian tariff on color television sets will range between 7.6% and 8.3%, depending on screen sizes, versus the 5% rate already in effect on all screen sizes in the United States. Conversely, the U.S. duty rate on color picture tubes will remain 15% while the Canadian Government will impose a 9.4% rate.

If under a bilateral free trade arrangement between the United States and Canada, the Japanese can funnel television receivers into the U.S. at a 5% duty rate for subsequent transshipment to Canada at no duty, we will have simply reduced the Canadian duty rate for the Japanese and injured ourselves in competing for business in Canada.

Conversely, if the Koreans continue to receive General Preferential tariff treatment, as they do in 1986, which allows them to import into Canada color TV receivers at 0% duty, then the Koreans can subsequently import their color

TV receivers duty free into the U.S. As a result, this proposed bilateral free trade arrangement would ultimately injure the U.S. industry, without safeguards.

Similarly, if the Japanese and Koreans can enter picture tubes into Canada at a 9.4% duty and move those tubes to the United States at zero duty rather than the U.S. 15% duty rate, we will have accomplished nothing for Canada and will have further injured an already import sensitive U.S. tube industry. This result can be avoided only if a free trade arrangement is limited to products that are genuinely of U.S. or Canadian origin. Otherwise, the Japanese and Koreans will merely be the principal benefactors.

In our negotiations with Canada, we should also be sensitive to the more recent Japanese and Korean export strategy. Our friends in the Far East export major television components for minor assembly operations in the U.S. in snap-together plants and then advertise these sets as domestic products, despite the absence of any significant North American labor or material content and certainly no domestic research, development and engineering. Based on current estimates, the Koreans are putting 1.6 million color sets together per year in such U.S. operations with about 500 U.S. employees.

These snap-together television receivers cannot be considered products of North American origin and unless substantial U.S. or Canadian labor or material is required in the finished television product, a bilateral free trade arrangement will turn into a duty-free bonus on products that essentially are Japanese or Korean in origin. In order to prevent this result, we urge that only products with at least 50% U.S. or Canadian content qualify for duty free treatment under any bilateral duty free arrangement. Anything less will provide an opportunity for evasion and will unnecessarily complicate customs administration.

If the Committee finds merit in my views on free and fair trade with Canada, I urge you to strongly recommend to the United States Trade Representative that our comments be taken into account in our Government's forthcoming bilateral trade negotiations.

Respectfully submitted,

Jerry K. Pearlman
Chairman and President
Zenith Electronics Corporation